TRANSCRIPT OF RECORD

Supreme Court of the United States

OCTOBER TERM, 1933

No. 44

JOHN T. DOBSON, PETITIONER,

vs.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE

No. 45

E. W. DOBSON, PETITIONER,

vs.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE

No. 46

ESTATE OF JAMES N. COLLINS, DECEASED, SECURITY NATIONAL BANK AND TRUST COMPANY OF MINNEAPOLIS, EXECUTOR, PETITIONER,

vs.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE

No. 47

E. J. HARWICK, PETITIONER,

vs.

COMMISSIONER OF INTERNAL REVENUE

IN THREE CASES BEFORE THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE EIGHTH CIRCUIT

PETITIONS FOR CERTIORARI FILED APRIL 24, 1934.

CERTIORARI GRANTED JUNE 4, 1934.

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1943

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vs.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE

No. 45

E. W. DOBSON, PETITIONER,

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GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE

No. 46

ESTATE OF JAMES N. COLLINS, DECEASED, FIRST NATIONAL BANK AND TRUST COMPANY OF MINNEAPOLIS, EXECUTOR, PETITIONER,

vs.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE

No. 47

H. J. HARWICK, PETITIONER,

vs.

COMMISSIONER OF INTERNAL REVENUE

ON WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE EIGHTH CIRCUIT

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[fol. a] [Caption omitted]

[fol. 1]

BEFORE UNITED STATES BOARD OF TAX APPEALS

DOCKET ENTRIES

Docket No. 105790

H. J. HARWICK, Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent

Appearances:

For Taxpayer: Leland W. Scott, John W. Windhorst.
For Comm'r: S. U. Hiken, Esq.

1940

Dec. 5—Petition received and filed. Taxpayer notified. (Fee paid).
Dec. 5—Copy of petition served on General Counsel.
Dec. 5—Request for circuit hearing in St. Paul, Minn., filed by taxpayer. 12/5/40 copy served.

1941

Jan. 27—Answer filed by General Counsel.
Jan. 30—Copy of answer served on taxpayer. (St. Paul, Minn.)
Apr. 28—Hearing set 6/16/41 (St. Paul, Minn.).
June 18—Hearing had before Mr. Turner on the merits. Submitted. Stipulation as to the facts filed. Brief due Aug. 2, 1941; Reply briefs Aug. 18, 1941.
July 25—Brief filed by taxpayer.
Aug. 2—Transcript of hearing 6/18/41 filed.
Aug. 2—Brief filed by General Counsel.
Aug. 4—Copy of brief served on General Counsel.

[fol. 2]

1942

Mar. 30—Memorandum opinion rendered, Turner, Div. 8. Decision will be entered under Rule 50. 3/30/42 copy served.

Apr. 17—Agree computation filed.
Apr. 23—Decision entered, Murdock, Div. 3.
July 20—Petition for review by United States Circuit Court of Appeals, Eighth Circuit, with assignments of error filed by taxpayer.
July 22—Proof of service filed.
Aug. 6—Agreed praecipe for transcript filed.

Petition of H. J. Harwick

Docket No. 105790

H. J. Harwick, Petitioner,

vs.

Commissioner of Internal Revenue, Respondent

Petition of H. J. Harwick

(Received and Filed December 5, 1942)

The above named Petitioner hereby petitions for a redetermination of the deficiency set forth by the Commissioner of Internal Revenue in his Notice of Deficiency dated October 21, 1940, and as a basis for the proceeding alleges as follows:

I

The Petitioner, H. J. Harwick, is an individual residing in the City of Rochester, County of Olmsted, State of Minnesota. On or about March 15, 1940, Petitioner filed an income tax return for the calendar year 1939 with the Collector of Internal Revenue of the United States in and for the District of Minnesota.

II

The Notice of Deficiency, a copy of which, marked Exhibit [fol. 3] A, is attached hereto and hereby made a part hereof, was mailed to Petitioner on October 21, 1940. The taxes in controversy are income taxes for the calendar year 1939 asserted against the Petitioner by said notice.

III

Said Notice of Deficiency determined that Petitioner's income tax liability for the calendar year 1939 was $38,272.72.

Of this amount $33,643.71 was paid by Petitioner during the calendar year 1940 and in addition $221.25 was paid on September 12, 1940. Respondent determined a deficiency in Petitioner's income tax liability for the calendar year 1939 in the sum of $4,629.01. The entire amount of said deficiency is in controversy.

IV

The determination of tax set forth in said Notice of Deficiency is based on the following errors:

(a) Respondent erred in determining that the entire amount of $17,000 recovered by Petitioner during the calendar year 1939 from National City Company constituted income taxable to Petitioner.

(b) Respondent erred in determining that $7,115.78 of said $17,000 received by Petitioner from National City Company did not constitute a return of capital to the Petitioner.

(c) Respondent erred in determining that Petitioner realized income in excess of the sum of $9,884.22 as a result of the recovery by Petitioner of said $17,000 from said National City Company.

(d) Respondent erred in determining that the income realized by Petitioner as a result of said recovery from National City Company did not constitute capital gain under the provisions of Section 117 of the Internal Revenue Code.

(e) Respondent erred in determining that there is a deficiency in Petitioner's income tax liability for the calendar year 1939.

V

The facts upon which Petitioner relies as a basis for this proceeding are as follows:

[fol. 4] (a) On or about July 22, 1929, the Petitioner purchased stock of National City Bank of New York from the National City Company for the sum of $38,100. On or about December 15, 1931, the Petitioner sold said stock for the sum of $3,648.72. The Petitioner thereby sustained a loss in the sum of $34,451.28. On or about March 15, 1932, Petitioner filed an income tax return for the calendar year

1931 with the Collector of Internal Revenue of the United States in and for the District of Minnesota. A true and correct copy of said return, marked Exhibit B, is attached hereto and hereby made a part hereof. The income deductions and credits set forth therein are true and correct and respondent has not made any changes therein.

(b) During the calendar year 1939 the Petitioner instituted suit against the National City Company for the recovery of the purchase price of said stock of the National City Bank of New York purchased from said National City Company on July 22, 1929, as set forth in paragraph V (a) above. Said suit was dismissed and Petitioner received as consideration for said dismissal the net amount of $17,000. Except for said recovery of $17,000 during the calendar year 1939 Petitioner has not been reimbursed in any manner for the loss sustained on the sale of said stock of National City Bank of New York realized upon sale thereof on December 15, 1931, as set forth in paragraph V (a) above.

Wherefore, Petitioner prays that this Board may hear the proceeding and decide that:

(a) Respondent erred in determining that the entire amount of $17,000 recovered by Petitioner during the calendar year 1939 from National City Company constituted income taxable to Petitioner.

(b) Respondent erred in determining that $7,115.78 of said $17,000 received by Petitioner from National City Company did not constitute a return of capital to the Petitioner.

(c) Respondent erred in determining that Petitioner realized income in excess of the sum of $9,884.22 as a result of the recovery by Petitioner of said $17,000 from said National City Company.

[fol. 5] (d) Respondent erred in determining that the income realized by Petitioner as a result of said recovery from National City Company did not constitute capital gain under the provisions of Section 117 of the Internal Revenue Code.

(e) Respondent erred in determining that there is a deficiency in Petitioner's income tax liability for the calendar year 1939.

Leland W. Scott, John W. Windhorst, 1300 First National-Soo Line Bldg., Minneapolis, Minnesota. Attorneys for Petitioner.

Duly sworn to by H. J. Hardwick. Jurat omitted in printing.

EXHIBIT "A" TO PETITION

Form 1230 SN-IT 1

Office of Internal Revenue Agent in Charge, St. Paul Division, 800 Post Office Bldg.

Treasury Department, Internal Revenue Service

St. Paul, Minnesota

[fol. 6] Oct. 21, 1940.

Collection District: Minnesota.

Mr. H. J. Harwick, c/o Mayo Clinic, Rochester, Minnesota

SIR:

You are advised that the determination of your income tax liability for the taxable year 1939 discloses a deficiency of $4,629.01 as shown in the statement attached.

In accordance with the provisions of existing internal revenue laws, notice is hereby given of the deficiency mentioned.

Within 90 days (not counting Sunday or a legal holiday in the District of Columbia as the 90th day) from the date of the mailing of this letter, you may file a petition with the United States Board of Tax Appeals for a redetermination of the deficiency.

Should you not desire to file a petition, you are requested to execute the enclosed form and forward it to the internal revenue agent in charge, St. Paul, Minnesota, for the attention of LGE-90D. The signing and filing of this form will

expedite the closing of your return(s) by permitting an early assessment of the deficiency, and will prevent the accumulation of interest, since the interest period terminates 30 days after filing the form, or on the date assessment is made, whichever is earlier.

Respectfully, Guy T. Helvering, Commissioner, by C. W. Rink, Internal Revenue Agent in Charge.

Enclosures: Statement. Form of waiver.
LGE/mrr.

GPO 2—17679

[fol. 7]

STATEMENT

Mr. H. J. Harwick,

c/o Mayo Clinic,

Rochester, Minnesota

Tax Liability for Taxable Year ended December 31, 1939

	Liability	Assessed	Deficiency
Income tax	$38,272.72	$33,643.71	$4,629.01

In making this determination of your income tax liability, careful consideration has been given to the report of examination dated July 10, 1940, to your protest dated September 3, 1940, and to statements made at conference held on October 7, 1940.

A copy of this letter and statement has been mailed to Leland W. Scott, 1300 First National Soo Line Building, Minneapolis, Minnesota, in accordance with the power of attorney executed by you.

Adjustments to Net Income

Net income as disclosed by return		$102,024.36
Unallowable deductions and additional income:		
(a) Trustees fees	$375.00	
(b) Recovery	7,115.78	7,490.78
Net income adjusted		109,515.14

Explanation of Adjustments

(a) This represents the inclusion in income of trustees' fees received from the First National Bank and Trust Company, co-trustee of Mayo Living Trust #2075.

(b) In 1939 you recovered $17,000.00 from the National City Bank in connection with your acquisition and sale of that stock in a prior year. This recovery constitutes gross income 100% taxable within the meaning of section 22(a) of the Internal Revenue Code. Accordingly that portion of the recovery not reported in your return is included herewith as taxable income as shown below:

[fol. 8] Total recovery	$17,000.00
Portion of recovery reported	9,884.22
Adjustment	7,115.78

Computation of Tax

Net income adjusted		$109,515.14
Less: Personal exemption	$2,500.00	
Credit for dependents	33.33	2,533.33
Balance (surtax net income)		106,981.81
Less: Earned income credit (10% of $14,000.00)		1,400.00
Net income subject to normal tax		105,581.81
Normal tax at 4% on $105,581.81		4,223.27
Surtax on $106,981.81		34,049.45
Total tax		38,272.72
Income tax assessed: Original, Account No. 200675		33,643.71
Deficiency of income tax		4,629.01

For Exhibit "B"

See Exhibit "B" attached to Stip Facts

United States Board of Tax Appeals

Docket No. 105790

H. J. HARWICK, Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent

ANSWER OF COMMISSSIONER OF INTERNAL REVENUE

(Received and Filed January 27, 1941)

[fol. 9] Now comes the Commissioner of Internal Revenue, by his attorney, J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue, and for answer to the petition filed herein admits and denies as follows:

I. Admits the allegations contained in paragraph I of the petition.

II. Admits the allegations contained in paragraph II of the petition except it is denied that the entire amount of the deficiency asserted in the deficiency notice is in controversy.

III. Admits that in the notice of deficiency it was determined that petitioner's income tax liability for the calendar year 1939 was $38,272.72; admits that respondent determined a deficiency in petitioner's income tax liability for the calendar year 1939 in the sum of $4,629.01; denies the remaining allegations contained in paragraph III of the petition.

IV. (a) to (e), inclusive. Denies that the respondent erred as alleged in subparagraphs (a) to (e), inclusive, of paragraph IV of the petition.

V. (a) Admits that on or about July 22, 1929, the petitioner purchased stock of National City Bank of New York for the sum of $38,100.00; admits that on or about December 15, 1931, the petitioner sold said stock for the sum of $3,648.72; admits that the petitioner thereby sustained a loss in the sum of $34,451.28; denies the remaining allega-

tions contained in subparagraph (a) of paragraph V of the petition.

V. (b) Denies the allegations contained in subparagraph (b) of paragraph V of the petition, except it is admitted that petitioner received $17,000.00 during 1939.

Denies generally and specifically each and every allegation contained in the petition not hereinbefore specifically admitted, qualified or denied.

Wherefore, respondent prays that the Board redetermine the deficiency herein to be the amount determined by the Commissioner, viz.: $4,629.01 in respect of income taxes for [fol. 10] the taxable year 1939.

J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue.

Of Counsel: F. R. Shearer, Division Counsel, S. U. Hiken, Special Attorney, Bureau of Internal Revenue.

UNITED STATES BOARD OF TAX APPEALS

Docket No. 105790

H. J. HARWICK, Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent

John W. Windhorst, Esq., and Leland W. Scott, Esq., for the petitioner.

S. U. Hiken, Esq., for the respondent.

OPINION

Turner: The respondent determined a deficiency in income tax for the year 1939 in the amount of $4,629.01. The question presented is whether a sum of money, or any part thereof, recovered by the petitioner in the taxable year as the result of a claim asserted against the National City Company of New York and arising out of a certain stock transaction in a prior year constitutes a return of capital, as contended by petitioner, or taxable income, as contended by the respondent. The parties have filed a written stipulation of facts with certain exhibits attached thereto and the

Board adopts such stipulation as its findings of fact. We shall recite only the facts deemed necessary to discussion of the issues presented.

Petitioner, a resident of Rochester, Minnesota, filed his 1939 income tax return with the collector of internal revenue for the district of Minnesota.

On July 22, 1929, the petitioner purchased, in a transaction entered into for profit, 100 shares of the capital stock of the National City Bank of New York. The stock also carried certain beneficial interests in the stock of the Na- [fol. 11] tional City Company of New York. The purchase was made in the State of Minnesota from the National City Company, the consideration being $38,000.

On December 15, 1931, petitioner sold the 100 shares of stock and sustained a loss by reason of said sale in the amount of $34,451.28. This loss was claimed as a deduction by the petitioner in his 1931 income tax return and was allowed by the respondent.

Until the early part of 1938 petitioner regarded the aforesaid purchase and sale as a closed and completed transaction. At that time he learned that other individuals who had purchased National City Bank stock in Minnesota from the National City Company had filed legal actions to recover the amounts paid by them for the stock on the ground that it had been sold without having been registered in accordance with the requirements of the Minnesota Blue Sky laws and on the ground that the sales had been fraudulent. After petitioner learned of these facts, and on or about January 10, 1939, he asserted a claim against the National City Company. On March 7, 1939, the claim was settled by a net payment of $17,000 by the company to petitioner, and upon receipt thereof, petitioner executed an instrument releasing the National City Company from all claims, demands, or causes of action which he ever had against it.

In his income tax return for 1939, the petitioner reported income of only $9,884.22 on account of the recovery of the $17,000. In the deficiency notice the respondent adjusted the amount of income reported by adding thereto $7,115.78, thereby treating the entire amount of petitioner's net recovery of $17,000 as gross income, taxable as ordinary gain. If the entire deduction of $34,451.28, claimed and allowed on petitioner's 1931 income tax return, had been disallowed, a deficiency in petitioner's income tax liability for 1931

would have resulted in the amount of $3,349.53, computed as follows:

Net income per return		$12,042.03
Add: Loss on sale of National City Bank stock		34,451.28
Net income revised		46,493.31

[fol. 12]

Less: Dividends	$11,861.81	
Personal exemption	3,500.00	
Credit for dependents	800.00	16,161.81
Balance subject to normal tax		$30,331.50
Normal tax:		
1-½% of first $4,000.00		60.00
3% of next $4,000.00		120.00
5% of $22,331.50		1,116.58
Total normal tax		$1,296.58
Surtax on $46,493.31		2,539.20
Total		$3,835.78
Less: Earned income credit		486.25
Total tax assessable		$3,349.53
Assessed		None
Deficiency		$3,349.53

If the petitioner had received $7,115.78 on the sale of the stock in 1931, in addition to the amount actually received, his deductible loss for 1931 from the sale of the said stock would have been $27,335.50 instead of $34,451.28, and he would have had net income in the amount of $19,157.81. Due to certain credits allowable, however, his income tax for 1931 would have been zero, shown as follows:

Net income shown in original return	$12,042.03
Add:	
Amount recovered in 1939 and not reported as taxable income for 1939	7,115.78
Net income revised	$19,157.81

Less: Dividends	$11,861.81	
Personal exemption	3,500.00	
Credit for dependents	800.00	16,161.81
Balance subject to normal tax		$ 2,996.00

[fol. 13]

Normal tax at 1-½%	44.94
Surtax on $19,157.81	186.30
Tax on net income	$ 231.24
Less earned income credit	231.24
Total tax assessable	00.00
Tax assessed	None
Deficiency	None

Throughout the year 1939 adjustment of petitioner's income tax liability for 1931 was barred by the statute of limitations.

Petitioner contends that the amount recovered in 1939 is in the nature of a capital recovery, and that it constitutes taxable income only to the extent that the loss deduction taken in 1931 resulted in a "tax benefit" to him. Of the total net recovery of $17,000, petitioner admits that to the extent of $9,884.22 he realized a "tax benefit" from the deduction taken in 1931, and concedes that to that extent the recovery constitutes taxable income for 1939. He contends, however, that the remaining $7,115.78 was of no "tax benefit" to him in 1931 and not therefore taxable income in 1939, since that amount could have been added to his gross income for 1931 without resulting in any income tax liability for such year. Petitioner also contends that if any portion of the recovery is taxable to him in 1939 it is taxable as capital gain. The respondent contends that the entire amount recovered in 1939 is taxable as ordinary gain and that it is wholly immaterial whether he realized any "tax benefit" from the deduction taken in 1931, but that in any event he realized a "tax benefit" to the full extent of the recovery, since the full amount of the deduction taken in 1931 did effect an offset of taxable income.

We have considered this same question in the case of Estate of James N. Collins, 46 B. T. A. ——— (March 27,

1942), and in that case we held that since the deduction claimed by the taxpayer in the prior year did not effect an offset of taxable income, the subsequent recovery in the taxable year did not constitute taxable income. In John V. Dobson, 46 B. T. A. —— (March 27, 1942), however, we [fol. 14] held that where recovery was had in a later year in respect of such loss the amount recovered was taxable income in the year of recovery to the extent that the deduction in the prior year of the amount later recovered had effected an offset of taxable income in such prior year. In the instant case the facts show that in 1931 petitioner was allowed a loss deduction of $34,451.28 on account of the sale of the bank stock and after taking such deduction he still had net income of $12,042.03. It appears therefore that the full amount of the deduction claimed in 1931 did effect an offset of taxable income. Accordingly the full amount recovered in 1939 is taxable income for that year. John V. Dobson, supra; National Bank of Commerce of Seattle v. Commissioner, 115 Fed. (2d) 875, affirming 40 B. T. A. 72; Central Loan and Investment Co., 39 B. T. A. 981; and Amsco-Wire Products Corporation, 44 B. T. A. 717.

Petitioner's contention that such income should be taxed as capital gain is denied on authority of Avery R. Schiller, 43 B. T. A. 594.

Decision will be entered under Rule 50.

Entered: March 30, 1942.

(Seal) U. S. Board of Tax Appeals, 1924.

UNITED STATES BOARD OF TAX APPEALS, WASHINGTON

Docket No. 105790

H. J. HARWICK, Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent.

ORDER OF REDETERMINATION

Pursuant to the Memorandum Opinion of the Board entered March 30, 1942, the parties herein having on April 17, [fol. 15] 1942, filed an agreed recomputation of tax in accordance therewith, it is

Ordered and Decided: That there is a deficiency in income tax for the year 1939 in the amount of $4,629.01.

Enter: Entered April 23, 1942.

J. E. Murdock, Member.

(Seal) U. S. Board of Tax Appeals, 1924.

UNITED STATES CIRCUIT COURT OF APPEALS, EIGHTH CIRCUIT

B. T. A. Docket No. 105790

H. J. HARWICK, Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE, Respondent.

PETITION OF H. J. HARWICK FOR REVIEW OF DECISION OF UNITED STATES BOARD OF TAX APPEALS—Filed July 20, 1042.

To The Honorable Judges of The United States Circuit Court of Appeals for the Eighth Circuit:

Now comes H. J. Harwick, by his attorneys, Leland W. Scott and John W. Windhorst, and respectfully shows:

I

JURISDICTION

The petitioner on review is an individual residing in the City of Rochester, County of Olmsted, State of Minnesota. The respondent on review holds his office under and by virtue of the laws of the United States. An income tax return was filed by the petitioner for the calendar year 1939 on or about March 15, 1940, with the Collector of Internal [fol. 16] Revenue for the District of Minnesota in St. Paul, Minnesota, whose office is located within the judicial district of the United States Circuit Court of Appeals for the Eighth Circuit.

II

NATURE OF CONTROVERSY

On October 21, 1940, the Respondent forwarded to the Petitioner by registered mail a notice of deficiency wherein the Petitioner was notified of a deficiency in the amount of $4,629.01 in his income tax liability for the year 1939.

Thereafter, on December 5, 1940, the Petitioner filed with the Board of Tax Appeals a petition for redetermination of the proposed deficiency for the year 1939. On January 27, 1941, the Commissioner filed with the Board of Tax Appeals his answer to the petition. The proceeding came on to be heard before a division of the Board of Tax Appeals sitting in St. Paul, Minnesota, on June 18, 1941.

The questions presented are (1) whether the Petitioner must include in his taxable gross income for the calendar year 1939 the amount of $7,115.78, representing a portion of the $17,000 received from National City Company in settlement of claim for rescission of a purchase of stock of National City Bank of New York under the Minnesota Blue Sky Law by the Petitioner and excluded by the Petitioner from income reported in his return and (2) whether the amount of said recovery which may be determined to constitute taxable income, including the portion which Petitioner concedes to be taxable, viz., $9,884.22, is taxable as ordinary income or as capital gain under Section 117 of the Internal Revenue Code.

On March 30, 1942, the Board of Tax Appeals promulgated its opinion wherein it was held that the Petitioner was taxable on the entire amount of $17,000 received in settlement of his claim against National City Company in 1939, including the sum of $7,115.78 which was excluded by the Petitioner from the taxable income reported in his return for 1939. The Board further held that said $17,000 was taxable as ordinary income rather than capital gain. On April 23, 1942, the Board entered its decision and [fol. 17] order that there was a deficiency of $4,629.01 in the Petitioner's income tax liability for the calendar year 1939. On or about April 14, 1942, the Petitioner paid the balance then owing of said deficiency, being $4,407.76, plus interest in the amount of $550.97, to the Collector of Internal Revenue for the District of Minnesota.

The facts, shortly stated, are as follows: On July 22, 1929, the Petitioner purchased from National City Company 100 shares of capital stock in the National City Bank of New York at a cost of $38,000. On December 15, 1931, Petitioner sold these shares for $3,648.72, sustaining a loss of $34,451.28, which amount was allowed by the Commissioner as a deduction in determining the Petitioner's income tax liability for that year. In 1938 Petitioner made a claim against the National City Company that he was entitled to

rescind the purchase of stock in 1929 and to recover the purchase price paid therefor. During the year 1939 this claim was compromised by the payment to Petitioner by National City Company of $17,000. Of this amount $7,115.78 was not included in the Petitioner's 1939 income tax return. The balance of $9,884.22 was included in Petitioner's 1939 income tax return as ordinary income and not as capital gain and a tax was paid thereon. If Petitioner's loss realized upon sale of said stock of National City Bank of New York in 1931 had been reduced by the amount of $7,115.78, his net income for 1931 Federal income tax purposes would have been $19,157.81. Due to deductions for personal exemption, credits for dependents, and the earned income credit, his income tax for 1931 on a net income of $19,157.81 would have been zero. The loss on the sale of said stock of National City Bank of New York in 1931 resulted in no tax saving to the Petitioner to the extent of $7,115.78.

III

Points on Which Petitioner Intends to Rely

Petitioner is aggrieved at the decision of the Board of Tax Appeals and says that in the proceeding before the Board and in the opinion and decision aforesaid manifest error occurred and intervened to his prejudice and he assigns as error the following:

[fol. 18] 1. The Board of Tax Appeals erred in determining that there was a deficiency in Petitioner's income tax liability for 1939 and in failing to order a refund to Petitioner for said year in the sum of $2,914.84, in that its decision is contrary to law.

2. The Board of Tax Appeals erred in finding that any part of the amount received in settlement of the legal claim against the National City Company in 1939 in excess of $9,884.22 was [includable] in the Petitioner's taxable income for the calendar year 1939, under Section 22 of the Internal Revenue Code.

3. The Board of Tax Appeals erred in finding that any part of the amount received in settlement of the claim against the National City Company in 1939 was to be treated as ordinary income rather than capital gain under Section 117 of the Internal Revenue Code.

4. The Board of Tax Appeals erred in failing to find that the said amount of $9,884.22 reported by Petitioner as ordinary income in his return for 1938 was taxable as capital gain under Section 117 of the Internal Revenue Code.

5. The Board of Tax Appeals erred in failing to find that none of the amount recovered in settlement of the legal claim against the National City Company in 1939 in excess of $9,884.22 was [includable] in the taxable income of the Petitioner in 1939, under Section 22 of the Internal Revenue Code.

6. The Board of Tax Appeals erred in entering judgment that there was a deficiency of $4,629.01 in the amount of the Petitioner's income tax liability for the calendar year 1939, instead of entering judgment of no deficiency for said year, together with a judgment for a refund to the Petitioner for said year in the sum of $2,914.84, in that the uncontradicted evidence warrants no other conclusion.

Wherefore, The Petitioner requests that the aforesaid decision of the Board of Tax Appeals be reviewed by the United States Circuit Court of Appeals for the Eighth Circuit; that a transcript of record be prepared in accordance with law and the rules of this Court and transmitted to the Clerk of said Court for filing; and that appropriate [fol. 19] action be taken, to the end that errors complained of may be reviewed and corrected by the Court.

Leland W. Scott, John W. Windhorst, Counsel for Petitioner, 1300 First National-Soo Line Building, Minneapolis, Minnesota.

Duly sworn to by John W. Windhorst, jurat omitted in printing.

* * * * * * *

In United States Circuit Court of Appeals

Notice of filing of Petition for Review and Service.

(Received and Filed July 22, 1942, United States Board of Tax Appeals.)

To: J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue.

You are hereby notified that H. J. Harwick did, on the 20th day of July, 1942, file with the Clerk of the United

States Board of Tax Appeals, at Washington, D. C., a [fol. 20] petition for review by the United States Circuit Court of Appeals for the Eighth Circuit, of the decision of the Board heretofore rendered in the above entitled case. Copy of the petition for review as filed is hereto attached and served upon you.

Dated this 21st day of July 1942.

B. D. Gamble, Clerk, U. S. Board of Tax Appeals.

Service of copy of Petition for Review acknowledged this 22nd July 1942.

J. P. Wenchel, Attorney for Respondent.

UNITED STATES BOARD OF TAX APPEALS

Docket No. 105790

H. J. HARWICK, Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent.

STIPULATION OF FACTS—Filed at Hearing June 18, 1941

It is hereby stipulated and agreed by and between the parties hereto, by their respective counsel, that the following facts shall be taken as true, provided, however, (1) that each of the parties hereto reserves the right to object to the admissibility in evidence of any of such facts, on the ground of irrelevancy and immateriality, and (2) that this stipulation shall be without prejudice to the right of either party to introduce other and further evidence not inconsistent herewith:

1. Petitioner, a resident of Rochester, Minnesota, filed, within the time required by law, his 1939 Federal income tax return with the Collector of Internal Revenue at St. Paul, Minnesota.

2. On July 22, 1929, Petitioner, in a transaction entered [fol. 21] into for profit, purchased in the State of Minnesota from the National City Company (of New York) 100

shares of the capital stock of National City Bank (hereinafter referred to as the stock) for $38,000, the purchase carrying with it, at no additional cost, a proportionate beneficial interest in the capital stock of National City Company (of New York). In June, 1933, the name of National City Company (of New York) was changed to City Company of New York, Inc.

3. On December 15, 1931, Petitioner sold the stock together with said beneficial interest in the capital stock of National City Company (of New York) for $3,648.72, thereby sustaining a loss of $34,451.28. This loss, which the Petitioner claimed as a deduction from gross income in his Federal income tax return for 1931, was allowed as a deduction by the Respondent.

4. From 1931 until the early part of 1938 the Petitioner regarded the aforesaid purchase and sale as a closed and completed transaction. In the early part of 1938, however, he learned that other individuals who had purchased National City Bank stock in Minnesota from the National City Company had filed legal actions to recover the amounts paid by them on the ground that the stock had been sold without having been registered in accordance with the requirements of the Minnesota Blue Sky laws and on the grounds that said sales had been fraudulent. After Petitioner made this discovery, and on or about January 10, 1939, he asserted a claim against the National City Company which was settled on March 7, 1939. The net amount which the petitioner received on such settlement, after paying attorneys fees and other similar expenses, was $17,000.00. A copy of the release which the Petitioner executed on such settlement is attached hereto, marked Exhibit A, and made a part hereof the same as if fully set forth herein.

5. In his Federal income tax return for 1939 the Petitioner reported income of only $9,884.22 on account of the receipt of $17,000.00 as aforesaid. In the deficiency notice from which the appeal herein was taken the Respondent adjusted the amount of income reported by the petitioner on said recovery by adding $7,115.78 thereto, thereby treating the entire amount of petitioner's net recovery of $17,000.00 as gross income, 100% taxable to the petitioner.

[fol. 22] 6. If the entire deduction of $34,451.28 which was claimed and allowed on Petitioner's 1931 Federal income tax return (paragraph 3, hereof, supra) had been disallowed, a deficiency in petitioner's Federal income tax liability for 1931 would have resulted in the amount of $3,349.53, computed as follows:

Net income per return		$12,042.03
Add: Loss on sale of National City Bank stock		34,451.28
Net income revised		$46,493.31
Less: Dividends	$11,861.81	
Personal exemption	3,500.00	
Credit for dependents	800.00	16,161.81
Balance subject to normal tax		$30,331.50
Normal tax:		
1½% of first $4,000.00		60.00
3% of next $4,000.00		120.00
5% of $22,331.50		1,116.58
Total normal tax		$ 1,296.58
Surtax on $46,493.31		2,539.20
Total		$ 3,835.78
Less: earned income credit		486.25
Total tax assessable		$ 3,349.53
Assessed		None
Deficiency		$ 3,349.53

Assessment of this deficiency was barred by statute of limitations throughout the year 1939.

7. If petitioner had received $7,115.78 on the sale of the stock in 1931 in addition to the $3,648.72 which he did receive (paragraph 3, hereof, supra,) his 1931 loss would have been $27,335.50 instead of $34,451.28, and his Federal income tax liability for 1931 would have been zero, computed as follows:

[fol. 23] 1931

Net income shown in original return		$12,042.03
Add:		
Amount recovered in 1939 and not report- as taxable income for 1939		7,115.78
Net income revised		$19,157.81
Less: Dividends	$11,861.81	
Personal exemption	3,500.00	
Credit for dependents	800.00	16,161.81
Balance subject to normal tax		$ 2,996.00
Normal tax at 1½%		44.94
Surtax on $19,157.81		186.30
Tax on net income		$ 231.24
Less earned income credit		231.24
Total tax assessable		00.00
Tax assessed		None
Deficiency		None

8. Photostats of the petitioner's Federal income tax returns for the years 1931 and 1939 are attached hereto, marked Exhibits B and C, respectively, and made a part hereof the same as if fully set forth herein. The income, deductions, and credits set forth in said return for the year 1931 are true and correct and Respondent has made no change therein upon audit of said return.

9. In the deficiency notice from which the appeal herein was taken the respondent disallowed a deduction designated as "trustee's fees," in the amount of $375.00, which the petitioner concedes to be correct.

10. Prior to the issuance of the deficiency notice herein the petitioner made a voluntary payment on account of his income tax liability for 1939 in the amount of $221.25.

This payment, which has not been assessed, is held in the suspense account of the Collector of Internal Revenue for [fol. 24] the District of Minnesota. The deficiency in Petitioner's income tax liability for 1939 which is asserted in the deficiency notice from which the appeal herein was taken is $4,629.01, but in view of said voluntary payment the amount of the deficiency in controversy is $4,401.12.

Leland W. Scott, John W. Windhorst, Counsel for Petitioner. J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue, Counsel for Respondent.

EXHIBIT "A" TO STIPULATION

Receipt and Release

For and in consideration of the sum of One Dollar ($1.00) and other good and valuable consideration, to me in hand paid by The City Company of New York, Incorporated, formerly The National City Company, I hereby release, discharge, and forever acquit said corporation, its subsidiaries and affiliates, and The National City Bank of New York and City Bank Farmers Trust Company, from all claims, demands, or causes of action which I ever had or now have against them, or any of them, arising directly or indirectly from any purchase whatsover from or any sale whatsoever by The National City Company or The City Company of New York, Incorporated, of stock or rights to subscribe to stock of The National City Bank of New York, or from subscriptions thereto, including any accompanying interest in the stock of The National City Company, The City Company of New York, Incorporated, or City Bank Farmers Trust Company.

In Witness Whereof, I have hereunto set my hand this 7th day of March, 1939.

H. J. Harwick.

In Presence of: ——— ———, ——— ———.

[fols. 25-26] STATE OF MINNESOTA,
County of Olmsted, ss:

On this 7th day of March, 1939, before me personally appeared H. J. Harwick to me known to be the person described in and who executed the foregoing instrument, and acknowledged that he executed the same as his free act and deed.

G. W. Shuster, Notary Public, Olmsted County, Minn. My Commission expires May 3, 1945. (Notarial Seal.)

EXHIBIT B to STIPULATION

Computation proved

INDIVIDUAL INCOME TAX RETURN

FOR NET INCOMES FROM SALARIES OR WAGES OF MORE THAN $5,000 AND INCOMES FROM BUSINESS, PROFESSION, RENTS, OR SALE OF PROPERTY

For Calendar Year 1931

File This Return With the Collector of Internal Revenue for Your District on or Before March 15, 1932

FIELD

Do Not Write In This Space

File No. 315

Serial Number M.i. 658964

District Minnesota

MAR 1932

ST. PAUL OFFICE

Cash Check M.O. Cert. of Int. Paid Payment

$

PRINT NAME AND ADDRESS PLAINLY BELOW

[redacted]

c/o Mayo Clinic

[redacted] Rochester Minn.

(Post office) (County) (State)

Occupation Business Executive

1. Are you a citizen or resident of the United States? Yes
2. If your filed a return for 1930, to what Collector's office was it sent? St. Paul, Minn.
3. Is this a joint return of husband and wife? Yes
4. If husband or wife filed a separate return, state when and where filed. -------
5. Were you married and living with husband or wife on the last day of your taxable year? M
6. If not, were you on the last day of your taxable year supporting in your household one or more persons closely related to you? ---
7. If your status in respect to questions 5 and 6 changed during the year, state date and nature of change. ----
8. How many dependent persons (other than husband or wife) under 18 years of age or incapable of self-support were receiving their chief support from you on the last day of your taxable year? Two

INCOME

1. Salaries, Wages, Commissions, etc. (State name and address of employer)	Amount received	Balance paid (Include on line 1)	
Mayo Clinic, Rochester, Minn.	$ 40,000.00	$	40 000 00
Kahler Corporation, Rochester, Minn.	10,076.25		10 076 25
Director's Fees			35 00
2. Income from Partnerships. (Name of Partnership)			
3. Interest on Bank Deposits, Notes, Corporation Bonds, etc. (except interest on tax-free covenant bonds)			50 00
4. Interest on Tax-free Covenant Bonds Upon Which a Tax was Paid at Source			
5. Income RECEIVED (State name and address) Mayo Clinic, Rochester, Minn.			4 161 68
OCT 6 1932			
ST. PAUL, MINNESOTA			
6. Rents and Royalties. (Form Schedule B)			
7. Profit from Sale of Real Estate, Bonds, etc. (Form Schedule C)			
8. Taxable Interest on Liberty Bonds, etc. (Form Schedule E)			
9. Dividends on Stock of Domestic Corporations			11 861 61
10. Other Income (including dividends on stock of foreign corporations). (State nature of income)			
(a) Warner Oil Syndicate			119 86
(b)			
11. Total Income or Items 1 to 11			16 378 32
DEDUCTIONS			
12. Interest Paid			3 812 25
13. Taxes Paid. (Explain in Schedule F) Real Estate, Pers.Prop. & Inc			1 396 07
14. Losses by Fire, Storm, etc. (Explain in Table at foot of page 4)			
15. Bad Debts. (Explain in Schedule F)			
16. Contributions. (Explain in Schedule F) 15% Limitation			2 125 07
17. Other Deductions Authorized by Law. (Explain in Schedule F)			
18. Total Deductions or Items 12 to 17			7 336 29
19. Net Income (Item 11 minus Item 18)			12 042 03

EARNED INCOME CREDIT

20. Earned Income (not over $30,000)	30000	00
21. Less Personal Exemption and Credit for Dependents	4300	00
22. Balance (Item 21 minus 20)	25700	00
23. Amount taxable at 1½% (not over $4,000)	4000	00
24. Amount taxable at 2% (not over $4,000)	4000	00
25. Amount taxable at 3% (Balance over $8,000 of Item 22)	17700	00
26. Normal Tax (1½% of Item 23)	60	00
27. Normal Tax (2% of Item 24)	120	00
28. Normal Tax (3% of Item 25)	885	00
29. Surtax on Item 21	880	00
30. Tax on Earned Net Income (total of Items 27 to 29)	1945	00
31. Credit of 20% of Tax (not over 20% of Items 26, 27, 28, and 29)	486	25

COMPUTATION OF TAX (See Instruction 22)

32. Net Income (Item 20 above)			12042 03
33. Liberty Bond Interest (Item 9)			
34. Dividends (Item 10)	11861	61	
35. Credit for Dependents	800	00	
36. Personal Exemption	3500	00	
37. Total of Items 33 to 36			16161 61
38. Balance (Item 32 minus 37)			NONE
39. Amount taxable at 1½% (not over $4,000)			
40. Balance (Item 32 minus 39)			
41. Amount taxable at 2% (not over $4,000)			
42. Amount taxable at 3% (Item 41 minus 42)			
43. Normal Tax (1½% of Item 39)			
44. Normal Tax (2% of Item 41)			
45. Normal Tax (3% of Item 42)			
46. Surtax on Item 32 (see Instruction 23)		20	42
47. Tax on Net Income (total of Items 43 to 46)			
48. Tax on Capital Gain or Loss (12½% of Col. 8, Sched. D)			
49. Total of or difference between Items 47 and 48		20	42
50. Less Credit of 20% of Tax on Earned Income (Item 29)		440	00
51. Total Tax (Item 50 minus 49)		NONE	
52. Less Income Tax Paid at Source			
54. Income Tax paid to a foreign country or U. S. possession			
55. Balance of Tax (Item 52 minus Items 53 and 54)		NONE	

AFFIDAVIT

I swear (or affirm) that this return, including the accompanying schedules and statements, has been examined by me, and to the best of my knowledge and belief, is a true and complete return made in good faith for the taxable year stated, pursuant to the Revenue Act of 1928 and the Regulations issued thereunder.

See Instruction 27

Sworn to and subscribed before me this 14 day of Feb 1932.

G C [illegible] TZ, Notary Public,
Rochester, Olmsted County, Minnesota.
My Com. [illegible] expires July 11, 1937

[redacted]

[redacted]

An amended return must be marked "Amended" at top of return. Checks and drafts will be accepted only if payable at par.

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27-28

SCHEDULE A—INCOME FROM BUSINESS OR PROFESSION (See Instruction 2)

1. Total receipts from business or profession (state kind of business) _____

Cost or Quoted Sales		Gross Receipts	
2. Labor			
3. Material and supplies			
4. Merchandise bought for sale			
5. Other costs (Itemize below or on separate sheet)			
6. Plus inventory at beginning of year			
7. Total (Lines 2 to 6)			
8. Less inventory at end of year			
9. Net Cost or Quoted Sales (Line 7 minus Line 8)			

Enter "C," or "C or M," on Lines 8 and 9 to indicate whether inventories are valued at cost, or cost or market, whichever is lower.

Explanation of deductions claimed on Lines 5 and 16 _____

Gross Receipts		Deductions	
10. Interest not included as "net income" and not deduct compensation		"Labor," in Line 2. (Do not deduct compensation for your services)	
11. Interest on business indebtedness		Indebtedness to others	
12. Taxes on business and business property		Business property	
13. Losses (explain in table at foot of page)			
14. Bad debts arising from sales or services			
15. Depreciation, obsolescence, and depletion (explain in table at foot of page)			
16. Rent, repairs, and other business expenses (Itemized below or on separate sheet)			
17. Total (Lines 10 to 16)			
18. Total Deductions (Line 9 plus Line 17)			
19. Net Profit (Line 1 minus Line 18) (Enter on Page 2)			

SCHEDULE B—INCOME FROM RENTS AND ROYALTIES (See Instruction 7)

1. Kind of Property	2. Amount Received	3. Cost or Value as of March 1, 1913, if Received Otherwise	4. Depreciation (Explain in table at foot of page)	5. Rentals	6. Gross Expenses (Itemize below)	7. Net Income (Enter on Line 3)

Explanation of deductions allowed in Column 6 _____

SCHEDULE C—PROFIT FROM SALE OF REAL ESTATE, STOCKS, BONDS, ETC. (See Instruction 8)

1. Kind of Property	2. Date Acquired	3. Amount Received	4. Depreciation Allowable Since Acquisition	5. Cost or Value as of March 1, 1913, if Received Otherwise	6. Improvements	7. Net Profit (Enter on Page 2)
Fairbanks Pfd Stk. 1800 Shs.	7-9-31	27875 00		40650 00		

Make how property was acquired _____

SCHEDULE D—CAPITAL NET GAIN OR LOSS FROM SALE OF ASSETS HELD MORE THAN TWO YEARS (See Instruction 9)

1. Kind of Property	2. Date Acquired	3. Date Sold	4. Amount Received	5. Depreciation Allowable Since Acquisition	6. Cost or Value as of March 1, 1913, if Received Otherwise	7. Improvements (Explain in table at foot of page)	8. Net Profit (Enter on Page 2)
	Mo. Day Year	Mo. Day Year					
Fed. City Bank-100 Shs	7-22-29	12-15-31	3646 72		3810 00		

Make how property was acquired _____

SCHEDULE E—INTEREST ON LIBERTY BONDS AND OTHER OBLIGATIONS OR SECURITIES (See Instruction 9)

1. Obligations or Securities	2. Interest Received or Accrued	3. Amount Owned	4. Interest Exempt from Taxation	5. Amount Owned at Beginning of Taxable Year	6. Amount Owned at Close of Taxable Year	7. Interest Received or Accrued During Taxable Year
(a) Obligations of a State, Territory, or political subdivision thereof, or the District of Columbia						
(b) Securities issued under Federal Farm Loan Act, or under such Act as amended, Treasury Bills, and Treasury Certificates of Indebtedness						
(c) Liberty 3½% Bonds and other obligations of United States issued on or before September 1, 1917, and obligations of U. S. possessions			All	******	******	******
(d) Liberty 4% and 4½% Bonds, Treasury Bonds, and Treasury Savings Certificates			All	******	******	******
			All	******	******	******
(e) Treasury Notes			66,000			
			None			

SCHEDULE F—EXPLANATION OF DEDUCTIONS CLAIMED IN ITEMS 1, 14, 16, 17, AND 18

17-Thru Mayo Clinic $3867.57 Y.M.C.A. $200.00 Church $200.00 Boy Scouts $200.00

Total--$3977.57

EXPLANATION OF DEDUCTION FOR DEPRECIATION CLAIMED IN SCHEDULES A AND B

1. Kind of Property (If building, state material of which constructed)	2. Date Acquired	3. Age When Acquired	4. Probable Life After Acquisition	5. Cost or Value as of March 1, 1913, if Received Otherwise (Exclusive of Land)	Amount of Depreciation Claimed and Allowed	
					6. Previous years	7. This year

EXPLANATION OF DEDUCTION FOR LOSSES BY FIRE, STORM, ETC., CLAIMED IN SCHEDULE A, AND IN ITEM 15

1. Kind of Property	2. Date Acquired	3. Cost or Value as of March 1, 1913, if Received Otherwise	4. Improvements	5. Depreciation Allowable Since Acquisition	6. Insurance and Salvage Value	7. Deductible Loss

EXHIBIT 6 to STIPULATION

FORM 1040
Treasury Department
Internal Revenue Service

UNITED STATES INDIVIDUAL INCOME TAX RETURN 1939

FOR NET INCOMES OF MORE THAN $5,000 FROM SALARIES, WAGES, DIVIDENDS, INTEREST, ANNUITIES, AND FOR INCOMES FROM OTHER SOURCES REGARDLESS OF AMOUNTS

For Calendar Year 1939

or fiscal year beginning 1-1-, 1939, and ended 1-1-, 1940

To be filed with the Collector of Internal Revenue for your district not later than the 15th day of the third month following the close of your taxable year

(Auditor's Stamp)

(Collector's Stamp)

File No. 200675

Serial [illegible]

District Minnesota

PRINT NAME AND ADDRESS PLAINLY. (See Instruction A)

H. J. Harwick - Attention: G. C. Utz
(Name) (If joint return, give first name of husband and wife)

Mayo Clinic
(Street and number, or rural route)

Rochester Olmsted Minnesota
(Post office) (County) (State)

Rec'd Int. Rev. Coll. St. P. MAR 12 1940

Field Check M.O.

Amount 9643.71

INCOME

1. Salaries and other compensation for personal services. (From Schedule A)	$ 89,469	00		
2. Dividends	14,899	50		
3. Interest on bank deposits, notes, mortgages, etc.	8	00		
4. Interest on corporation bonds				
5. Taxable interest on Government obligations, etc. (From Schedule B)				
6. Income (or loss) from partnerships, syndicates, pools, etc. (other than capital gains or losses). (Furnish names and addresses): Warner Syndicate	74	98		
7. Income from fiduciaries. (Furnish names and addresses):				
8. Rents and royalties. (From Schedule C)				
9. Income (or loss) from business or profession. (From Schedule D)				
10. (a) Net short-term gain from sale or exchange of capital assets. (From Schedule F)				
(b) Net long-term gain (or loss) from sale or exchange of capital assets. (From Schedule F)				
(c) Net gain (or loss) from sale or exchange of property other than capital assets. (From Schedule C) Recovery on National City Bank Stock Loss	9,884	22		
11. Other income (including income from annuities) (State nature)				
Total income in items 1 to 11. (Enter corresponding income in Schedule D)			$ 111,352	36

RECD INT. REV. COLL. OF MINN. DIST. MAR 13 1940 ST. PAUL OFFICE

DEDUCTIONS

13. Contributions paid. (Explain in Schedule H)	$ 2,014	16		
14. Interest. (Explain in Schedule H)	120	00		
15. Taxes. (Explain in Schedule H)	7,194	04		
16. Losses from fire, storm, shipwreck, or other casualty, or theft. (Explain in Schedule H)				
17. Bad debts. (Explain in Schedule H)				
18. Other deductions authorized by law. (Explain in Schedule H)				
19. Total deductions in items 13 to 18			9,328	20
20. Net income (item 12 minus item 19)			$ 102,024	36

COMPUTATION OF TAX

21. Net income (item 20 above)			$ 102,024	36	28. Normal tax (4% of item 27)		$ 3,923	64
22. Less: Personal exemption. (From Schedule J-1)	$ 2500	00			29. Surtax on item 24. (See Instruction 29)		29,720	07
23. Credit for dependents. (From Schedule J-2)	33	33	2,533	33	30. Total (item 28 plus item 29)		$ 33,643	71
24. Balance (surtax net income)			$ 99,491	02	31. Total tax (item 30, or if you had a net long-term capital gain or loss, enter line 14, Schedule F)		$	
25. Less: Interest on Government obligations, etc. (See Instruction 25)	$				32. Less: Income tax paid at source	$		
26. Earned income credit. (From Schedule K-1 or K-2)	1400	00	1,400	00	33. Income tax paid to a foreign country or U.S. possession (Attach Form 1116)			
27. Balance subject to normal tax			$ 98,091	02	34. Balance of tax (item 31 minus items 32 and 33)		$	

NOTE.—One form marked "DUPLICATE COPY" must be filed with this original return ($5 will be assessed if duplicate copy is not filed)

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Schedule A—[illegible] LIST OF SALARIES, WAGES, FEES, AND OTHER [illegible] (See Instruction 7)

1. Name and address of employer or nature of business	2. Amount	3. Nature (Insert)	4. Amount
Mayo Clinic, Rochester	76,270 86	Traveling Expense	$ 641 00
[illegible] Corporation, Rochester	$20,000 00		
Wabash, Ind.	108 00		
First Nat'l Bank Minneapolis	160 00		
Total of column 2 minus total of column 4 (enter as item 1, page 1)			$ 86,489 86

Schedule B.—INTEREST ON GOVERNMENT OBLIGATIONS, ETC. (See Instruction C)

1. Obligations or securities	2. Amount owned at end of year (including your proportionate share of such obligations held by estates, trusts, partnerships, or common trust funds)	3. Interest received or credited during the year	4. Interest exempt from taxation	5. Interest on amount in column 2 if taxable
(a) Obligations of a State, Territory, or political subdivision thereof, or the District of Columbia, or United States possessions	$	$	All	
(b) Obligations issued under Federal Farm Loan Act, or under such Act as amended			All	
(c) Obligations of United States issued on or before September 1, 1917			All	
(d) Treasury Notes, Treasury Bills, and Treasury Certificates of Indebtedness			All	
(e) United States Savings Bonds and Treasury Bonds			$	$
(f) Obligations of instrumentalities of the United States (other than obligations to be reported in (b) above)			None	
(g) Total (enter as item 5, page 1)				$

Schedule C.—INCOME FROM RENTS AND ROYALTIES. (See Instruction 8)

1. Kind of property	2. Amount	3. Depreciation (explain in Schedule E)	4. Repairs (explain below)	5. Other expenses (itemize below)	6. Net profit (subtract 3, 4, and 5 from 2) (enter as item 8, page 1)
	$	$	$	$	$

Explanation of deductions claimed in columns 4 and 5 .....

Schedule D.—PROFIT (OR LOSS) FROM BUSINESS OR PROFESSION. (See Instruction 9)

(State business name and address if different from name and address on page 1 .....)

1. Total receipts (state nature of business or profession) ..... $

COST OF GOODS SOLD		OTHER BUSINESS DEDUCTIONS	
2. Labor	$	10. Salaries not included as "Labor" (do not deduct compensation for yourself)	$
3. Material and supplies		11. Interest on business indebtedness	
4. Merchandise bought for sale		12. Taxes on business and business property	
5. Other costs (itemize below)		13. Losses (explain below)	
6. Plus inventory at beginning of year		14. Bad debts arising from sales or services	
7. Total (lines 2 to 6)	$	15. Depreciation, obsolescence, and depletion (explain in Schedule E)	
8. Less inventory at end of year		16. Rent, repairs, and other expenses (itemize below or on separate sheet)	
9. Net cost of goods sold (line 7 minus line 8)	$	17. Total (lines 10 to 16)	$
		18. Total deductions (line 9 plus line 17)	
		19. Net profit (or loss) (line 1 minus line 18) (enter as item 9, page 1)	$

If the production, manufacture, purchase and sale of merchandise is an income-producing factor, inventories are required. Enter "L," or "C or M," on lines 6 and 8 to indicate whether inventories are valued at cost, or cost or market, whichever is lower.

Explanation of deductions claimed in lines 5, 13, and 16 .....

Schedule E.—EXPLANATION OF DEDUCTION FOR DEPRECIATION CLAIMED IN SCHEDULES C, D, F, AND G

1. Kind of property (If buildings, state material of which constructed)	2. Date acquired	3. Cost or other basis	4. Amount fully depreciated as of end of year	5. Depreciation allowed (or allowable) in prior years	6. Remaining cost or other basis to be recovered	7. Estimated life used in accumulating depreciation	8. Estimated remaining life from beginning of year	9. Depreciation allowable this year
		$	$	$	$			$

10 over

Schedule F.—GAINS AND LOSSES FROM SALES OR EXCHANGES OF CAPITAL ASSETS. (See Instructions 10)

1. Kind of property (If necessary, attach separate sheet and identify each item listed)	2. Date acquired (Mo. Day Year)	3. Date sold (Mo. Day Year)	4. Gross sales price (contract price)	5. Cost or other basis	6. Expenses of sale and cost of improvements subsequent to expenditures or March 1, 1913	7. Depreciation allowed (or allowable) since acquisition or March 1, 1913 (explain in Schedule E)	8. Gain or loss (subtract item 6 plus column 4 of Schedule E from item 5 and 7)	Gain or loss to be taken into account: 9. Percentage	10. Amount
SHORT-TERM CAPITAL GAINS AND LOSSES—ASSETS HELD NOT MORE THAN 18 MONTHS									
			$	$	$	$	$	100	$
								100	
								100	
								100	
Total net short-term capital gain or loss (enter in line 1, column 3, of summary below)									$
LONG-TERM CAPITAL GAINS AND LOSSES—ASSETS HELD FOR MORE THAN 18 MONTHS BUT NOT FOR MORE THAN 24 MONTHS									
			$	$	$	$	$	66⅔	$
								66⅔	
								66⅔	
								66⅔	
LONG-TERM CAPITAL GAINS AND LOSSES—ASSETS HELD FOR MORE THAN 24 MONTHS									
			$	$	$	$	$	50	
								50	
								50	
								50	
Total net long-term capital gain or loss (enter in line 2, column 3, of summary below)									$

SUMMARY OF CAPITAL NET GAINS OR LOSSES

1. Classification	2. Net short-term capital loss of preceding taxable year (not in excess of net income for such year)	3. Net gain or loss to be taken into account from column 10, above		4. Net gain or loss to be taken into account from partnerships and "common trust funds"		5. Total net gain or loss to be taken into account for columns 2, 3, and 4 of this summary	
		Gain	Loss	Gain	Loss	Gain	Loss
1. Total net short-term capital gain or loss (enter as item 10 (a), page 1, amount of gain shown in column 5)	$	$	$	$	$	$	No net loss allowable (see Instruction 10)
2. Total net long-term capital gain or loss (enter as item 10 (b), page 1, amount of gain or loss shown in column 5)		$	$	$	$	$	$

State the family, fiduciary, or business relationship to you, if any, of purchaser of any of the above items: _____

If any of the above items were acquired by you other than by purchase, explain fully how acquired: _____

COMPUTATION OF ALTERNATIVE TAX
(To be used only in the case of a net long-term capital gain or loss)

1. Net income (item 28, page 1). (See Instruction 10)	$	10. Normal tax (4% of line 9)	$
2. (a) Net long-term capital gain (item 10 (b), page 1)		11. Surtax on line 6. (See Instruction 29)	
(b) Net long-term capital loss (item 10 (b), page 1)		12. Partial tax (line 10 plus line 11)	$
3. Ordinary net income (line 1 minus line 2 (a) or line 1 plus line 2 (b)). (See Instruction 10)		13. (a) 30% of net long-term capital gain (30% of line 2 (a))	
4. Less: Personal exemption. (From Schedule J-1)	$	(b) 30% of net long-term capital loss (30% of line 2 (b))	
5. Credit for dependents. (From Schedule J-2)		14. Alternative tax (line 12 plus line 13 (a) or line 12 minus line 13 (b))	$
6. Balance (surtax net income)	$	15. Total normal tax and surtax (item 30, page 1)	$
7. Less: Interest on Government obligations, etc. (See Instruction 25)	$	16. Tax liability (if a net long-term capital gain, on line 2 (a), enter line 14 or line 15, whichever is the lesser; if a net long-term capital loss, on line 2 (b), enter line 14 or line 15, whichever is the greater). (Enter as item 31, page 1)	$
8. Earned income credit. (From Schedule K-1 or K-2). (See Inst. 10)			
9. Balance subject to normal tax	$		

Schedule G.—GAINS AND LOSSES FROM SALES OR EXCHANGES OF PROPERTY OTHER THAN CAPITAL ASSETS
(See Instruction 10)

1. Kind of property	2. Date acquired	3. Gross sales price (contract price)	4. Cost or other basis	5. Expenses of sale and cost of improvements subsequent to expenditures or March 1, 1913	6. Depreciation allowed (or allowable) since acquisition or March 1, 1913 (explain in Schedule E)	7. Gain or loss (subtract item 5 plus column 4 minus the sum of columns 4 and 5)
		$	$	$	$	$
Total net gain (or loss) (enter as item 10 (c), page 1)						$

State the family, fiduciary, or business relationship to you, if any, of purchaser of any of the above items: _____

If any of the above items were acquired by you other than by purchase, explain fully how acquired: _____

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Schedule H.—EXPLANATION OF DEDUCTIONS CLAIMED IN ITEMS 20, 21, AND 24

Item No.	1. Deduction	2. Amount		Item No.	3. Recipient (Name)	4. Amount	
15	Real Estate Tax	$ 1,894	10	13	Episcopal Church	$ 454	16
15	Personal Property Tax	210	37	13	Boy Scouts	700	00
15	Excise Tax	85	00	13	Red Cross	10	00
15	Auto Tax	54	37	13	University of Minnesota	500	00
15	State Income	5,560	20	13	Community Chest	250	00
		7,194	04	13	Minn. Medical Foundation	100	00

Schedule I.—NONTAXABLE INCOME OTHER THAN INTEREST REPORTED IN SCHEDULE B. (See Instruction G) $2,014.16

1. Source of Income	2. Nature of Income	3. Amount
		$

Schedule J.—EXPLANATION OF CREDITS CLAIMED IN ITEMS 22 AND 23. (See Instructions 22 and 23)

(1) Personal Exemption

Status	Number of months during the year in each status	Credit claimed
Single, or married and not living with husband or wife		$
Married and living with husband or wife	12	2,500 00
Head of family (explain below)		

(2) Credit for Dependents

Name of dependent and relationship	Number of months during the year: Under 18 years old	Number of months during the year: Over 18 years old	Credit claimed
Mary Anne, Daughter	1		$ 33 33

Reason for support if over 18 years old

Schedule K.—COMPUTATION OF EARNED INCOME CREDIT. (See Instruction 26)

(1) If your net income is $3,000 or less, use only this part of schedule

Net income (item 20, page 1)	$
Earned income credit (10% of net income, above)	

(2) If your net income is more than $3,000, use only this part of schedule

Earned net income (not more than $14,000)	$
Net income (item 20, page 1)	
Earned income credit (10% of earned net income or 10% of net income, above, whichever amount is smaller, but do not enter less than $300)	

QUESTIONS

1. State your principal occupation or profession Business Manager
2. Check whether you are a citizen ☒ or a resident alien ☐.
3. If you filed a return for the preceding year, to which Collector's office was it sent? St. Paul
4. Are items of income or deductions of both husband and wife included in this return? No
5. State (a) Name of husband or wife if separate return was made
   (b) Personal exemption, if any, claimed thereon
   (c) Collector's office to which it was sent
6. Check whether this return was prepared on the cash ☒ or accrual ☐ basis.
7. Did you at any time during your taxable year own directly or indirectly any stock of a foreign corporation or a personal holding company as defined by section 501? (Answer "yes" or "no") No (If answer is "yes," attach statement required by Instruction J.)

AFFIDAVIT. (See Instruction E)

I/we swear (or affirm) that this return (including any accompanying schedules and statements) has been examined by me/us, and to the best of my/our knowledge and belief is a true, correct, and complete return, made in good faith, for the taxable year stated, pursuant to the Internal Revenue Code, as amended, and the regulations issued under authority thereof.

Subscribed and sworn to by H. J. Hanwick before me this 7 day of Feb 1940

G. O. [illegible], Notary Public
Rochester, Minn.
My Commission Expires

(Signature) (See Instruction E)

(Signature)

(If this is a joint return (not made by agent), it must be signed by both husband and wife. It must be sworn to before a proper officer by the spouse preparing the return. If neither or both prepare the return, it must be sworn to by both spouses.)

If made abroad by an agent must be accompanied by power of attorney. (See Instruction E.)

AFFIDAVIT. (See Instruction E)

(If this return was prepared for you by some other person, the following affidavit must be executed)

I/we swear (or affirm) that I/we prepared this return for the person or persons named herein and that the return (including any accompanying schedules and statements) is a true, correct, and complete statement of all the information respecting the income tax liability of the person or persons for whom this return has been prepared of which I/we have any knowledge.

Subscribed and sworn to before me this ..... day of ....., 194

(Signature and title of officer administering oath)

(Signature of person preparing the return)

(Signature of person preparing the return)

(Name of firm or employer, if any)

U. S. GOVERNMENT PRINTING OFFICE 16—6054

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[fol. 39] BEFORE UNITED STATES BOARD OF TAX APPEALS

PRAECIPE FOR TRANSCRIPT—Filed August 6, 1942

To the Clerk of the United States Board of Tax Appeals:

You are requested by the petitioner in the above entitled action to prepare, transmit, and deliver to the Clerk of the United States Circuit Court of Appeals for the Eighth Circuit copies, duly certified as correct, of the following documents and records in the above entitled cause in connection with the Petition for Review heretofore filed by said petitioner:

1. Docket entries of proceedings before the Board.

2. Pleadings before the Board.

3. Opinion of the Board promulgated March 30, 1942.

4. Decision filed April 23, 1942.

5. Petition for Review, together with notice of filing thereof and proof of service.

6. The stipulation of facts agreed upon between the parties.

7. This Praecipe.

Dated August 6, 1942.

Leland W. Scott, John W. Windhorst. Agreed to:
J. P. Wenchel, Attorney for Respondent.

UNITED STATES BOARD OF TAX APPEALS, WASHINGTON

Docket No. 105790

H. J. HARWICK, Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent

CLERK'S CERTIFICATE TO TRANSCRIPT

[fol. 40] I, B. D. Gamble, clerk of the U. S. Board of Tax Appeals, do hereby certify that the foregoing pages, 1 to

34, inclusive, contain and are a true copy of the transcript of record, papers, and proceedings on file and of record in my office as called for by the Praecipe in the appeal as above numbered and entitled.

In testimony whereof, I hereunto set my hand and affix the seal of the United States Board of Tax Appeals, at Washington, in the District of Columbia, this 19th day of August, 1942.

B. D. Gamble, Clerk, United States Board of Tax Appeals. Filed Aug. 29, 1942, E. S. Kock, Clerk. (Seal: U. S. Board of Tax Appeals, 1924.)

IN THE UNITED STATES CIRCUIT COURT OF APPEALS, FOR THE EIGHTH CIRCUIT

ORDER CONSOLIDATING CASES FOR BRIEFING, HEARING, ARGUMENT AND DECISION AND AS TO PRINTING OF RECORDS—September 10, 1942

[Title omitted]

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* * * * * * *

[fol. 41] Come Now the parties to the above entitled proceedings, by their counsel of record, and it is

Ordered, that the above entitled proceedings be consolidated for briefing, hearing, argument and decision; that one brief shall be filed on behalf of the Commissioner and one on behalf of the four taxpayers; that the first brief shall be filed by the Commissioner and that it shall be filed within forty days after the date on which the last transcript of record is filed with the Clerk of this Court in the cases in which the Commissioner has filed petitions for review; that the second brief shall be filed on behalf of the taxpayers twenty-five days after their receipt of the Commissioner's brief, in accordance with the rules of this Court; that in order to facilitate handling of these proceedings and also to provide a fair and practicable method of dividing costs, the transcripts of record in the three cases appealed by the Commissioner shall be consolidated for printing and be printed by the Commissioner when his brief is printed; that such record shall include, in the case of John

V. Dobson, all the material needed to consider both of the issues referred to above with the exception of the cross-petition for review which shall be printed as hereinafter indicated; that the transcript of record in H. J. Harwick v. Commissioner and the cross-petition in the case of John V. Dobson shall be printed together by the taxpayers therein with the cost of printing to be divided between them as [fol. 42] they shall decide; and that the latter record shall be printed by the taxpayers in sufficient time for it to be available for use by counsel for Commissioner in preparation of his brief, or they shall furnish a copy of the record to be printed to counsel for Commissioner in ample time for his use.

September 10, 1942.

[fol. 42-A] UNITED STATES CIRCUIT COURT OF APPEALS, EIGHTH CIRCUIT

B. T. A. Docket No. 106553

JOHN V. DOBSON, Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE, Respondent

PETITION OF JOHN V. DOBSON FOR REVIEW OF DECISION OF UNITED STATES BOARD OF TAX APPEALS—Filed July 20, 1942, United States Board of Tax Appeals

To the Honorable Judges of the United States Circuit Court of Appeals for the Eighth Circuit:

Now comes John V. Dobson, by his attorneys, Leland W. Scott and John W. Windhorst, and respectfully shows:

I

JURISDICTION

The petitioner on review is an individual residing in the City of Minneapolis, County of Hennepin, State of Minnesota. The respondent on review holds his office under and by virtue of the laws of the United States. An income tax return was filed by the Petitioner for the calendar year 1939 on or about March 15, 1940, with the Collector of Internal

Revenue for the District of Minnesota in St. Paul, Minnesota, whose office is located within the judicial district of the United States Circuit Court of Appeals for the Eighth Circuit.

II

Nature of Controversy

On December 26, 1940, the Commissioner forwarded to the Petitioner by registered mail a notice of deficiency [fol. 42-B] wherein the Petitioner was notified of a deficiency in the amount of $9,108.06 in his income tax liability for the year 1939.

Thereafter, on March 3, 1941, the Petitioner filed with the Board of Tax Appeals a petition for redetermination of the proposed deficiency for the year 1939. On March 31, 1941, the Commissioner filed with the Board of Tax Appeals his answer to the petition of the Petitioner. The proceeding came on to be heard before a division of the Board of Tax Appeals sitting in St. Paul, Minnesota, on June 18, 1941.

The questions presented are (1) whether the Petitioner must include in his taxable gross income for the calendar year 1939 the amount of $2,251.49 representing a portion of the amount received in settlement of a suit for rescission of a purchase of National City Bank of New York stock by the Petitioner from National City Company, and (2) if said amount is to be included in Petitioner's taxable income for 1939, whether it is to be treated as ordinary income or as capital gain under Section 117 of the Internal Revenue Code.

On March 27, 1942, the Board of Tax Appeals promulgated its opinion wherein it was held that the Petitioner was taxable on the amount of $2,251.49 of the total received in settlement of damage suits in 1939 and excluded by the Petitioner from the taxable income reported in his return for 1939. The Board further held that said $2,251.49 was taxable as ordinary income rather than capital gain. On April 22, 1942, the board entered its decision and order that there was a deficiency of $472.82 in the Petitioner's income tax liability for the calendar year 1939. On or about April 28, 1942, the Petitioner paid the entire amount of said deficiency, plus interest in the amount of $60.27, to the Collector of Internal Revenue for the District of Minnesota.

The facts shortly stated are as follows: At various times in 1929 the petitioner purchased from National City Com-

pany a total of 440 shares of capital stock in the National City Bank of New York. During 1930 the Petitioner sold a portion of this stock for $20,897.44. This stock had cost the Petitioner $83,168.44 and Petitioner thereby sustained a loss on said stock in the sum of $62,271, which amount was allowed by the Commissioner as a deduction in deter- [fol. 42-C] mining the Petitioner's income tax liability for 1930. In 1938 Petitioner commenced a suit against the National City Company wherein he sought to rescind the purchase of the stock for alleged fraud on the part of the defendant and violations of the Minnesota Blue Sky Law. The action was settled during the year 1939 by a net payment of $33,404 by the National City Company to the Petitioner. Of the amount received in settlement, $32,294.96 is allocable to the stock sold by the Petitioner in 1930. This latter amount was not included in the taxable income reported by Petitioner in his 1939 income tax return. If the deductible loss suffered during 1930 upon the sale of National City Bank stock were reduced by the amount of 1939 recovery allocable to the shares sold during 1930, the 1930 income tax return of the Petitioner would have shown a net income of $2,251.49. Because of a personal exemption in the amount of $3500 and a credit for dependents in the amount of $1200, the tax liability of the Petitioner for 1930 under these circumstances would have been zero. The loss on the stock sales in 1930, to the extent compensated for by the 1939 settlement, resulted in no tax saving to the Petitioner.

III

Points Upon Which Petitioner Intends to Rely

Petitioner is aggrieved at the decision of the Board of Tax Appeals and says that in the proceeding before the Board and in the opinion and decision aforesaid manifest error occurred and intervened to his prejudice and he assigns as error the following:

1. The Board of Tax Appeals erred in determining that there is a deficiency of $472.82 in Petitioner's income tax liability for 1939, in that its decision is contrary to law.

2. The Board of Tax Appeals erred in finding that a part of the amount received in settlement of the legal action against the National City Company in 1939, to the extent

of $2,251.49, was [includable] in the Petitioner's taxable income for the calendar year 1939 under Section 22 of the Internal Revenue Code.

3. The Board of Tax Appeals erred in finding that a part [fol. 42-D] of the amount received in settlement of the legal action against the National City Company in 1939 in the amount of $2,251.49 was to be treated as ordinary income rather than capital gain under Section 117 of the Internal Revenue Code.

4. The Board of Tax Appeals erred in failing to find that none of the amount recovered in settlement of the legal action against the National City Company in 1939 and allocable to the purchase price of stock of National City Bank of New York which was sold in 1930 was [includable] in the taxable income of the Petitioner in 1939, under Sec. 22 of the Internal Revenue Code.

5. The Board of Tax Appeals erred in entering judgment that there was a deficiency of $472.82 in the amount of Petitioner's income tax liability for the calendar year 1939, instead of entering judgment of no deficiency for said year, in that the uncontradicted evidence warrants no other conclusion.

Wherefore, The Petitioner requests that the aforesaid decision of the Board of Tax Appeals be reviewed by the United States Circuit Court of Appeals for the Eighth Circuit; that a transcript of record be prepared in accordance with law and the rules of this Court and transmitted to the Clerk of said Court for filing; and that appropriate action be taken to the end that errors complained of may be reviewed and corrected by the Court.

Leland W. Scott, John W. Windhorst, Counsel for Petitioner, 1300 First National-Soo Line Building, Minneapolis, Minnesota.

* * * * * * *

Duly sworn to by John W. Windhorst, Jurat omitted in printing.

[fol. 42-E] IN UNITED STATES CIRCUIT COURT OF APPEALS, FOR THE EIGHTH CIRCUIT

B. T. A. Docket No. 106553

JOHN V. DOBSON, Petitioner on Review

vs.

COMMISSIONER OF INTERNAL REVENUE, Respondent on Review

To: J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue.

NOTICE OF FILING OF PETITION FOR REVIEW BY JOHN V. DOBSON AND ACKNOWLEDGMENT OF SERVICE

(Received and Filed July 22, 1942, United States Board of Tax Appeals)

You are hereby notified that John V. Dobson did, on the 20th day of July, 1942, file with the Clerk of the United States Board of Tax Appeals, at Washington, D. C., a petition for review by the United States Circuit Court of Appeals for the Eighth Circuit, of the decision of the Board heretofore rendered in the above entitled case. Copies of the petition for review and the statement of points as filed are hereto attached and served upon you.

Dated this 21st day of July 1942.

B. D. Gamble, Clerk U. S. Board of Tax Appeals.

[fol. 42-F] Service of copy of Petition for Review and Statement of Points acknowledged this July 22, 1942.

J. P. Wenchel, Attorney for Respondent.

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UNITED STATES BOARD OF TAX APPEALS, WASHINGTON

Docket No. 106553

COMMISSIONER OF INTERNAL REVENUE, Petitioner,

v.

JOHN V. DOBSON, Respondent

Docket No. 106553

JOHN V. DOBSON, Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent

CLERK'S CERTIFICATE TO TRANSCRIPT

I, B. D. Gamble, clerk of the U. S. Board of Tax Appeals, do hereby certify that the foregoing pages, 1 to 76, inclusive, contain and are a true copy of the transcript of record, papers, and proceedings on file and of record in my office as called for by the Praecipe in the appeal (or appeals) as above numbered and entitled.

In testimony whereof, I hereunto set my hand and affix the seal of the United States Board of Tax Appeals, at Washington, in the District of Columbia, this 25th day of August, 1942.

B. D. Gamble, Clerk, United States Board of Tax Appeals.

Filed Sept. 2, 1942. E. E. Koch, Clerk.

(Seal) Board of Tax Appeals, 1924.

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* * * * * * *

[fol. 42-G] IN THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE EIGHTH CIRCUIT

[Title omitted]

ORDER CONSOLIDATING CASES FOR BRIEFING, HEARING, ARGUMENT AND DECISION AND AS TO PRINTING OF RECORDS—September 10, 1942

Come Now the parties to the above entitled proceedings, by their counsel of record, and it is

Ordered, that the above entitled proceedings be consolidated for briefing, hearing, argument and decision; that

one brief shall be filed on behalf of the Commissioner and one on behalf of the four taxpayers; that the first brief shall [fol. 42-H] be filed by the Commissioner and that it shall be filed within forty days after the date on which the last transcript of record is filed with the Clerk of this Court in the cases in which the Commissioner has filed petitions for review; that the second brief shall be filed on behalf of the taxpayers twenty-five days after their receipt of the Commissioner's brief, in accordance with the rules of this Court; that in order to facilitate handling of these proceedings and also to provide a fair and practicable method of dividing costs, the transcripts of record in the three cases appealed by the Commissioner shall be consolidated for printing and be printed by the Commissioner when his brief is printed; that such record shall include, in the case of John V. Dobson, all the material needed to consider both of the issues referred to above with the exception of the cross-petition for review which shall be printed as hereinafter indicated; that the transcript of record in H. J. Harwick v. Commissioner and the cross-petition in the case of John V. Dobson shall be printed together by the taxpayers therein with the cost of printing to be divided between them as they shall decide; and that the latter record shall be printed by the taxpayers in sufficient time for it to be available for use by counsel for Commissioner in preparation of his brief, or they shall furnish a copy of the record to be printed to counsel for Commissioner in ample time for his use.

September 10, 1942.

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[fols. 1-3] UNITED STATES BOARD OF TAX APPEALS

Docket No. 106566

COMMISSIONER OF INTERNAL REVENUE, Petitioner

v.

ESTATE OF JAMES N. COLLINS, DECEASED, FIRST NATIONAL BANK AND TRUST COMPANY OF MINNEAPOLIS, EXECUTOR, Respondent

ORDER ENLARGING TIME

Upon motion of counsel for petitioner, it is ordered that the time for preparation, transmission and delivery of the

record sur petition for review of the above-entitled proceeding in the United States Circuit Court of Appeals for the Eighth Circuit is extended to October 12, 1942.

(Signed) J. E. Murdock, Member.

Dated: Washington, D. C., August 13, 1942.
eeh.

Now, September 2, 1942 the foregoing order is certified from the record as a true copy.

B. D. Gamble, Clerk, U. S. Board of Tax Appeals.

[Endorsed:] Filed in U. S. Circuit Court of Appeals on September 4, 1942.

Before United States Board of Tax Appeals

Docket No. 106566

James N. Collins (Amended Title—Estate of James N. Collins, Deceased, First National Bank and Trust Company of Minneapolis), Executor, Petitioner

v.

Commissioner of Internal Revenue, Respondent

Appearances: For Taxpayer: Leland W. Scott, John W. Windhorst. For Comm'r: Jonas Smith, Esq., S. U. Hiken, Esq.

[fol. 4] Docket Entries

1941
Mar. 3—Petition received and filed. Taxpayer notified. Fee paid.
Mar. 3—Copy of petition served on General Counsel.
Mar. 3—Request for Circuit hearing in St. Paul, Minnesota, filed by taxpayer. 3/3/41 copy served.
Mar. 31—Answer filed by General Counsel.
Apr. 3—Copy of answer served on taxpeyer. (St. Paul, Minnesota.)
Apr. 28—Hearing set June 16, 1941, St. Paul, Minnesota.
June 9—Motion for substitution of petitioner filed by taxpayer.

June 9—Order that henceforth the caption of this proceeding shall be Estate of James N. Collins, Deceased, First National Bank and Trust Company of Minneapolis, Executor, entered.

June 18—Hearing had before Mr. Turner on motion of respondent to file amended answer. Granted. Amended answer. Copy served.

June 18—Hearing had before Mr. Turner on the merits submitted. Stipulation as to the facts filed. Briefs due Aug. 2, 1941. Reply briefs Aug. 18, 1941.

July 25—Brief filed by taxpayer.

July 28—Motion for extension to Aug. 15, 1941, to file brief filed by General Counsel. 7/31/41 granted.

Aug. 2—Transcript of hearing 6/18/41 filed.

Aug. 11—Motion for extension of time to Aug. 30, 1941, to file briefs filed by General Counsel. 8/14/41 granted.

Aug. 29—Brief filed by General Counsel.

Sept. 2—Copy of brief served on General Counsel.

Sept. 13—Reply brief filed by taxpayer. 9/15/41 copy served.

1942

Mar. 27—Opinion rendered. Turner, Div. 8. Decision will be entered under Rule 50. 3/30/42 copy served.

Apr. 22—Agreed computation of deficiency filed.

Apr. 25—Decision entered. Arthur Mellott, Div. 11.

July 14—Petition for review by U. S. Circuit Court of Appeals, 8th Circuit, with assignments of error filed by General Counsel.

July 21—Proof of service filed by General Counsel.

Aug. 13—Motion for extension of time to 10/12/42 within which to prepare, transmit, and deliver the record filed by General Counsel.

[fol. 5] Aug. 13—Order enlarging time to Oct. 12, 1942, to prepare, transmit, and deliver the record entered.

Aug. 21—Praecipe for record filed by General Counsel, with proof of service thereon.

United States Board of Tax Appeals

Docket No. 106566

JAMES N. COLLINS, Petitioner

vs.

COMMISSIONER OF INTERNAL REVENUE, Respondent

Received Mar. 3, 1941. U. S. Board of Tax Appeals.

PETITION

The above-named Petitioner hereby petitions for a redetermination of the deficiency set forth by the Commissioner of Internal Revenue in his Notice of Deficiency dated February 18, 1941, and as a basis for the proceeding alleges:

I.

The Petitioner, James N. Collins, is an individual residing in the City of Minneapolis, County of Hennepin, State of Minnesota. On or about March 15, 1940, Petitioner filed an income tax return for the calendar year 1939 with the Collector of Internal Revenue of the United States in and for the District of Minnesota.

II

The Notice of Deficiency, a copy of which, marked Exhibit A, is attached hereto and hereby made a part hereof, was mailed to Petitioner on February 18, 1941. The taxes in controversy are income taxes for the calendar year 1939 asserted against the Petitioner by said notice.

III

The Notice of Deficiency determined that Petitioner's income tax liability for the calendar year 1939 was $2,331.04. No part of this has been paid by the Petitioner and Respondent determined a deficiency in Petitioner's income tax liability for the calendar year 1939 in said sum of $2,331.04. The entire amount of said deficiency is in controversy.

[fol. 6]

IV

The determination of tax set forth in said Notice of Deficiency is based on the following errors:

(a) Respondent erred in determining that $29,750.63, out of the net amount of $45,150.63 recovered by Petitioner during the calendar year 1939 from National City Company, constituted income taxable to the Petitioner.

(b) Respondent erred in determining that the entire amount of said $45,150.63 recovered by Petitioner from National City Company did not constitute a return of capital to the Petitioner.

(c) Respondent erred in determining that Petitioner realized any income as the result of the recovery by Petitioner of said $45,150.63 from said National City Company.

(d) If the Petitioner realized income as the result of said recovery from National City Company, Respondent erred in determining that said income did not constitute capital gain under the provisions of Section 117 of the Internal Revenue Code.

(e) Respondent erred in determining that there is a deficiency in Petitioner's income tax liability for the calendar year 1939.

V

The facts upon which Petitioner relies as a basis for this proceeding are as follows:

(a) On or about the dates and for the amounts set forth below the Petitioner purchased and sold stock of National City Bank of New York:

1. On January 2, 1929, Petitioner purchased 5 shares at a cost of $1,325.

2. On April 8, 1929, Petitioner purchased 85 shares at a cost of $31,875.

3. On May 27, 1929, Petitioner purchased 10 shares at a cost of $3,900.

4. On October 14, 1929, Petitioner purchased 100 shares at a cost of $56,200.

5. On November 11, 1929, Petitioner purchased 100 shares at a cost of $30,000.

6. On August 29, 1930, Petitioner sold the 100 shares purchased at item 4 above for $14,599.20.

7. On April 22, 1931, Petitioner sold the 5 shares of stock purchased at item 1 above for the sum of $446.81.

[fol. 7] 8. On April 22, 1931, Petitioner sold the 10 shares of stock purchased at item 3 above for $893.62.

9. On April 22, 1931, Petitioner sold the 85 shares purchased at item 2 above for $7,595.79.

(b) On or about March 15, 1931, the Petitioner filed with the Collector of Internal Revenue of the United States in and for the District of Minnesota an income tax return for the calendar year 1930. The net income disclosed by said return, exclusive of losses realized by the sale of capital assets, was $19,830.13. During the calendar year 1930 the Petitioner sold securities other than stock of National City Bank of New York and realized a loss on said sale in the net amount of $44,125.84. On or about August 29, 1930, Petitioner sold 100 shares of the stock of National City Bank of New York, as set forth at item V (a) 6 above. Petitioner thereby realized a loss of $41,600.80. Said loss was reported by Petitioner in his income tax return for said calendar year 1930. The income and deductions set forth in Petitioner's income tax return for the calendar year 1930 are a true and correct statement of Petitioner's net income for said year and Respondent has not made any changes therein.

(c) On or about March 15, 1932, Petitioner filed an income tax return for the calendar year 1931 with the Collector of Internal Revenue of the United States in and for the District of Minnesota. In said return Petitioner disclosed the following gross income and deductions therefrom:

Income:		
Salaries	$21,639.12	
Interest	10,586.89	
Rents and royalties	275.09	
Dividends on stock of domestic corporations	11,117.47	
Miscellaneous income and directors' fees	756.51	
Total income		$44,375.08

Deductions:		
Interest paid	$2,346.69	
Taxes paid	1,492.56	
Contributions	1,112.30	
Loss on sale of stocks and bonds other than stock of National City Bank of New York	51,454.65	
Loss on sale of stock of National City Bank of New York	28,163.78	
Total Deductions		84,579.98
Net income		None

The income and deductions set forth above are a true and correct statement of Petitioner's net income for the calendar year 1930 and the Respondent has not made any changes [fol. 8] therein. The loss sustained on the sale of stock of National City Bank of New York in the sum of $28,163.78, described in said return, was realized from the sale of 100 shares of said stock for the sum of $8,936.22, as set forth at items V (a) 7, 8, and 9 above. Said stock was acquired by Petitioner at a cost of $37,100, as set forth at items V (a) 1, 2, and 3 above.

(d) During the calendar year 1939 the Petitioner instituted suit against the National City Company for the recovery of the purchase price of the stock of National City Bank of New York purchased from National City Company on April 8, 1929, May 27, 1929, October 14, 1929, and November 11, 1929, as set forth in paragraph V (a) 2, 3, 4, and 5 above. Said suit was dismissed and Petitioner received, during the calendar year 1939, as consideration for said dismissal, the net amount of $45,150.63. The sum of $6,454.18 was recovered with respect to the 85 shares of stock purchased on April 8, 1929 (item V (a) 2 above), and 10 shares of stock purchased on May 27, 1929 (item V (a) 3 above); $23,296.45 was recovered with respect to the 100 shares of stock purchased on October 14, 1929 (item V (a) 4 above); and $15,400 was recovered with respect to the 100 shares of stock purchased on November 11, 1929, (item V (a) 5 above).

(e) Except for said recovery of $45,150.63 during the calendar year 1930, Petitioner has not been reimbursed in any manner for the loss sustained on the sale of stock of

National City Bank of New York as set forth in paragraph V (a) above.

Wherefore, petitioner prays that this Board may hear the proceeding and decide that:

(a) Respondent erred in determining that $29,750.63, out of the net amount of $45,150.63 recovered by Petitioner during the calendar year 1939 from National City Company, constituted income taxable to the Petitioner.

(b) Respondent erred in determining that the entire amount of said $45,150.63 recovered by Petitioner from National City Company did not constitute a return of capital to the Petitioner.

(c) Respondent erred in determining that Petitioner realized any income as the result of the recovery by Petitioner of said $45,150.63 from said National City Company.

(d) If the Petitioner realized income as the result of said recovery from National City Company, Respondent erred in determining that said income did not constitute capital gain under the provisions of Section 117 of the Internal Revenue Code.

[fol. 9] (e) Respondent erred in determining that there is a deficiency in Petitioner's income tax liability for the calendar year 1939.

Leland W. Scott, Leland W. Scott, John W. Windhorst, John W. Windhorst, 1300 First National-Soo Line Bldg., Minneapolis, Minnesota, Attorneys for Petitioner.

Duly sworn to by James N. Collins. Jurat omitted in printing.

EXHIBIT "A" TO PETITION

SN-IT-1

Office of Internal Revenue Agent in Charge, St. Paul Division, 800 Post Office Bldg.

Treasury Department, Internal Revenue Service, St. Paul, Minnesota, Feb. 18, 1941.

Collection District: Minnesota

Mr. James N. Collins,
c/o Roy F. Hooker,
924 Baker Building, Minneapolis, Minnesota.

SIR: You are advised that the determination of your income tax liability for the taxable year (x) 1939 discloses a deficiency of $2,331.04 as shown in the statement attached.

In accordance with the provisions of existing internal revenue laws, notice is hereby given of the deficiency mentioned.

Within 90 days (not counting Sunday or a legal holiday in the District of Columbia as the 90th day) from the date [fol. 10] of the mailing of this letter, you may file a petition with the United States Board of Tax Appeals for a redetermination of the deficiency.

Should you not desire to file a petition, you are requested to execute the enclosed form and forward it to the Internal Revenue Agent in Charge, St. Paul, Minnesota for the attention of LGE-90D. The signing and filing of this form will expedite the closing of your return(s) by permitting an early assessment of the deficiency, and will prevent the accumulation of interest, since the interest period terminates 30 days after filing the form, or on the date assessment is made, whichever is earlier.

Respectfully,
Guy T. Helvering, Commissioner. By C. W. Rink,
Internal Revenue Agent in Charge.

Enclosures: Statement. Form of waiver. LGE/mrr.

STATEMENT

Mr. James N. Collins, c/o Roy F. Hooker, 924 Baker Building, Minneapolis, Minnesota

Tax Liability for Taxable Year Ended January 3, 1941

Income tax: Liability, $2,331.04; assessed, None; deficiency, $2,331.04.

In making this determination of your income tax liability, careful consideration has been given to the report of examination dated January 3, 1941.

Investigation disclosed that there is allowable a credit for one dependent only, namely, your sister, Mrs. W. C. Winslow.

Adjustments to Net Income

Net income (loss) as disclosed by return	($6,833.41)
Unallowable deductions and additional income:	
(a) Recovery	29,750.63
Net income adjusted	22,917.22

Explanation of Adjustments

(a) In 1939 you recovered $45,150.63 as a result of a suit against the National City Company, due to illegal sales of [fol. 11] stock by that company. No portion of this recovery was included as taxable income in your return. It is held that the net recovery in connection with that stock previously sold constitutes taxable income in its entirety, and that the recovery on stock retained during 1939 constitutes a reduction in the cost basis of same.

	Total stock	Stock retained	Stock previously disposed of
Recovery, 84% of loss	$67,725.95	$23,100.00	$44,625.95
Attorney fees	22,575.32	7,700.00	14,875.32
Net recovery	45,150.63	15,400.00	29,750.63

Computation of Tax

Adjusted net income		$22,917.22
Less:		
Personal exemption	$1,000.00	
Credit for dependents	400.00	1,400.00
Surtax net income		21,517.22
Less: Earned income credit		300.00
Balance subject to normal tax		21,217.22
Normal tax at 4%		848.69
Surtax		1,487.58
Total tax		2,336.27
Less: Income tax paid at source		5.23
Total tax assessable		2,331.04
Tax previously assessed: Account No. 656162		None
Deficiency of income tax		2,331.04

UNITED STATES BOARD OF TAX APPEALS

Docket No. 106566

JAMES N. COLLINS, Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent

Received Mar. 31, 1941. U. S. Board of Tax Appeals

ANSWER

Now comes the Commissioner of Internal Revenue, by his attorney, J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue, and for answer to the petition filed herein, admits, denies and alleges:

[fol. 12] I, II, and III. Admits the allegations contained in paragraphs I, II, and III of petition.

IV. (a) to (e), inclusive. Denies that the respondent erred as alleged in subparagraphs (a) to (e), inclusive, of paragraph IV of the petition.

V. (a) Admits that sometime prior to 1939 the petitioner purchased and sold stock of National City Bank; denies the remaining allegations contained in subparagraph (a) of paragraph V of the petition.

V. (b) Admits that sometime prior to 1939 the petitioner sold stock of National City Bank; admits that petitioner realized a loss on said sale, the exact amount of which is unknown to the respondent; denies the remaining allegations contained in subparagraph (b) of paragraph V of the petition.

V. (c) Denies the allegations contained in subparagraph (c) of paragraph V of the petition.

V. (d) Admits that during the calendar year 1939 the petitioner instituted a suit against the National City Company; admits that petitioner received the net amount of $45,150.63 in 1939 on account of the institution of said suit; denies the remaining allegations contained in subparagraph (d) of paragraph V of the petition.

V. (e) Denies the allegations contained in subparagraph (e) of paragaph V of the petition.

Denies generally and specifically each and every allegation contained in the petition not hereinbefore specifically admitted, qualified or denied.

Wherefore, respondent prays that the Board redetermine the deficiency herein to be the amount determined by the Commissioner, viz.: $2,331.04 in respect of income taxes for the taxable year 1939.

(Signed) J. P. Wenchel, S. U. H., J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue.

Of counsel: F. R. Shearer, Division Counsel. S. U. Hiken, Special Attorney, Bureau of Internal Revenue.

[fol. 13] UNITED STATES BOARD OF TAX APPEALS

Docket No. 106566

JAMES N. COLLINS, Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent

AMENDED ANSWER—*Filed at hearing June* 16, 1941

Now comes the Commissioner of Internal Revenue, by his attorney, J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue, and for amended answer to the petition filed herein admits, denies and alleges:

I, II, and III. Admits the allegations contained in paragraphs I, II, and III of petition.

IV. (a) to (e), inclusive. Denies that the respondent erred as alleged in subparagraphs (a) to (e), inclusive, of paragraph IV of the petition.

V. (a) Admits that sometime prior to 1939 the petitioner purchased and sold stock of National City Bank; denies the remaining allegations contained in subparagraph (a) of paragraph V of the petition.

V. (b) Admits that sometime prior to 1939 the petitioner sold stock of National City Bank; admits that petitioner realized a loss on said sale, the exact amount of which is unknown to the respondent; denies the remaining allega-

tions contained in subparagraph (b) of paragraph V of the petition.

V. (c) Denies the allegations contained in subparagraph (c) of paragraph V of the petition.

V. (d) Admits that during the calendar year 1939 the petitioner instituted a suit against the National City Company; admits that petitioner received the net amount of $45,150.63 in 1939 on account of the institution of said suit; denies the remaining allegations contained in subparagraph (d) of paragraph V of the petition.

V. (e) Denies the allegations contained in subparagraph (e) of paragraph V of the petition.

Denies generally and specifically each and every allegation contained in the petition not hereinbefore specifically admitted, qualified or denied.

VI. Further answering, and by way of affirmative allegation, respondent alleges that he erred in determining the amount of deficiency in income tax due from the petitioner [fol. 14] herein for the year 1939 in that he should have disallowed the following deductions which were claimed in the petitioner's return but not disallowed in the deficiency notice:

Item	Amount
Office expenses, including bookkeeping, postage, etc.	$221.46
Agent's Salary	500.00
Attorneys' Fees	210.00
1st National Bank & Trust Co. Advisory Service	573.68
Safety Deposit Box rent	9.00
Total	1,514.14

VII. The facts upon which the respondent relies in support of said allegation of error are as follows:

(a) On information and belief, it is alleged that the aforementioned items were claimed as deductions by the petitioner as business expenses on the theory that the petitioner was engaged in a trade or business in 1939.

(b) On information and belief, it is alleged that the petitioner was not engaged in a trade or business during the year

1939 and that the aforesaid items were not paid or incurred in the operation of a business by the petitioner and hence do not constitute expenditures which are deductible from gross income.

(c) On information and belief, it is alleged that the petitioner's activities throughout 1939, on account of which the foregoing expenditures were made, consisted only of the performance of such acts as were necessary to look after and manage petitioner's personal investments.

Wherefore, it is prayed that petitioner's appeal be denied and that the deficiency for the year 1939 be redetermined by adding to the adjusted net income appearing in the statement attached to the deficiency notice from which the appeal herein was taken the amount of $1,514.14 as set forth in paragraph VI and subparagraphs (a) to (c), inclusive, of paragraph VII of this answer. Claim is hereby asserted for the increased deficiency for the year 1939 resulting from such redetermination.

(Signed) J. P. Wenchel, D. A. T., J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue.

Of Counsel: F. R. Shearer, Division Counsel; S. U. Hiken, Special Attorney, Bureau of Internal Revenue.

[fol. 15] UNITED STATES BOARD OF TAX APPEALS

ESTATE OF JAMES N. COLLINS, DECEASED, FIRST NATIONAL BANK AND TRUST COMPANY OF MINNEAPOLIS, EXECUTOR, Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent

Docket No. 106566. Promulgated March 27, 1942

In 1929 the decedent purchased in the State of Minnesota certain bank stock from the National City Co. of New York. In 1930 and 1931 he sold the stock for less than its purchase price and in his returns for those years claimed deductions for the losses so sustained. The returns for the said years would have disclosed net losses even if the deductions in respect of the above stock sales had not been claimed. In 1936 decedent learned that the bank stock had not been registered in accordance with the Minnesota Blue Sky Laws

and in 1937 filed suit against the company for rescission of the contract. The suit was settled by compromise and in 1939 the company paid a sum of money to the decedent as full settlement. The purchase price of the stock paid by decedent exceeds the proceeds of the 1930 and 1931 sales plus the amount recovered in 1939. *Held,* the money recovered in 1939 does not constitute taxable income to the decedent.

John W. Windhorst, Esq., for the petitioner.
S. U. Hiken, Esq., for the respondent.

OPINION

Turner: The respondent determined a deficiency in income tax for 1939 in the amount of $2,331.04. The issue is whether a sum of money recovered by the decedent in the taxable year as a result of litigation involving certain stock transactions in prior years constitutes a return of capital, as contended by petitioner, or taxable income, as contended by the respondent. The parties have filed a written stipulation of facts, with certain exhibits attached thereto, and the Board adopts such stipulation as its findings of fact. We shall recite only the facts deemed necessary to the discussion of the issue presented.

The decedent, James N. Collins, died on April 21, 1941, a resident of Hennepin County, State of Minnesota. He filed his income tax return for 1939 with the collector of internal revenue at St. Paul, Minnesota. The petitioner is the duly appointed executor of his estate.

[fol. 16] In 1929 the decedent purchased 300 shares of the capital stock of the National City Bank of New York. The stock also carried certain beneficial interests in the stock of the National City Co. of New York. The purchase was made in the State of Minnesota from the National City Co. In 1930 the decedent sold 100 shares of the stock, which had cost him $56,200, for $14,599.20, thereby sustaining a deductible loss for Federal income tax purposes in the amount of $41,600.80. This loss was claimed as a deduction in his 1930 return and was allowed by the respondent. In 1931 the decedent sold 100 shares of the stock, which had cost him $37,100, for $8,936.22, thereby sustaining a deductible loss for income tax purposes in the amount of $28,163.78. This loss was claimed as a deduction in his 1931 return and was allowed by the respondent. The remaining 100 shares

of stock referred to were still owned by the decedent at the time of his death.

Until the fall of 1936 the decedent regarded the aforesaid purchases and sales as closed and completed transactions. During that fall he learned for the first time that the stock had not been registered in accordance with the requirements of the Minnesota Blue Sky Laws and further learned of facts which led him to believe that the sales by the company to him might have been fraudulent. On August 23, 1937, he filed suit against the National City Co. in an effort to recover the amounts which he paid for the stock, alleging that the stock had been sold to him without having been registered in accordance with the requirements of the Minnesota Blue Sky Laws and that the sales had been fraudulent. He asked for a rescission of the entire transaction and tendered to the defendant company the proceeds of said stock, or an equivalent number of shares of stock of the bank, plus interest and dividends received.

In 1939 the suit was settled by a payment of $67,725.95 by the company to the decedent, such amount representing 84 percent of the losses he had sustained in his dealings with the stock. After deducting attorney's fees and other expenses in connection with the suit, the decedent had a net recovery of $45,150.63. On March 28, 1939, the suit was dismissed, with prejudice, pursuant to stipuation of the parties. Of the total net recovery, $29,750.63 is allocable to the stock sold by the decedent in 1930 and 1931, of which $23,296.45 is allocable to the stock sold in 1930 and the balance of $6,454.18 is allocable to the stock sold in 1931.

If the entire deductions of $41,600.80 for 1930 and $28,163.78 for 1931, claimed and allowed on the decedent's returns for those years, had been disallowed, the returns [fol. 17] still would have shown net losses for those years. If the decedent had received $23,296.45 on the sale of the stock in 1930 in addition to the amount actually received on such sale, and if he had received $6,454.18 on the said of the stock in 1931 in addition to the amount actually received on such sale, his 1930 and 1931 net losses would have been $42,600.06 and $33,750.72, respectively, and he would have had no income tax liability for either year.

Throughout the taxable year 1939 adjustment of the decedent's income tax liability for 1930 and 1931 was barred by the statute of limitations.

In his income tax return for 1939 the decedent did not report as income any portion of the recovery received from the National City Co. In the deficiency notice the respondent adjusted the amount of gross income reported by adding thereto and treating as ordinary gain the amount of $29,750.63 representing that portion of the net recovery which was attributable to the shares of stock sold by the decedent in 1930 and 1931. He did not add that portion of the recovery which was attributable to the 100 shares of stock which had not been disposed of by the decedent.

Petitioner contends that the suit brought by the decedent against the National City Co. was in the nature of an action for rescission of the original contract and that the amount recovered in 1939 is in the nature of a capital recovery which does not constitute taxable income in the absence of realization of gain, either actually or constructively, and that he realized no gain, since the deductions claimed in the years when the stock was sold did not result in any "tax benefits" to him. In the alternative, petitioner contends that, if the amount recovered is taxable to the decedent, it is taxable as capital gain. The respondent contends that the entire amount recovered by the decedent from the company is taxable as ordinary gain and that it is wholly immaterial whether he realized any "tax benefits" from the deductions taken in the prior years.

We think the record supports the petitioner's contention that the suit brought by the decedent was in the nature of an action for rescission of the original contract, as distinguished from an action for damages. In the complaint he prayed for a rescission of the entire transaction and the return of the purchase price of the stock, and he tendered the proceeds of the stock, or an equivalent number of shares of stock, plus interest and dividends received. Had the suit been disposed of in the regular procedure and resulted in a court order placing the parties in status quo, it would seem that the purchase price thus recovered by petitioner [fol. 18] would represent a return of capital, rather than taxable income. But the suit was not disposed of in that manner. It was settled by a stipulated compromise, the company paying an amount of money to the decedent. True, the decedent had already sold the stock in 1930 and 1931, but that fact does not require the conclusion that the transactions were completely closed at that time because the decedent still maintained his right of action against the

company. Moreover, regarding the series of transactions as a whole, it is apparent that no gain was actually realized by the decedent. The purchase price which he paid for the stock is in excess of the proceeds realized from the sales in 1930 and 1931 plus the total net recovery in 1939. Therefore, it seems to us that the real question presented is whether the fact that the decedent sold the stock in 1930 and 1931 and claimed deduction in his returns for those years, for which he realized no tax benefits, requires us to hold that the amount recovered in 1939 constitutes taxable income, even though he realized no economic gain.

In Burnet v. Canford & Brooks Co., 282 U. S. 359, which case is strongly relied upon by the respondent, the taxpayer entered into a contract with the United States Government for dredging the Delaware River. In its income tax returns from 1913 to 1916 it added to gross income for each year the payments received under the contract and deducted its expenses paid in performing the contract. The total expenses exceeded the payments received and its returns for 1913, 1915, and 1916 showed net losses. Its return for 1914 showed net income. In 1915 work under the contract was abandoned and in 1916 the taxpayer brought suit to recover for a breach of warranty of the character of the material to be dredged. It obtained judgment in the Court of Claims, the court stating that the recovery was upon the contract and was "compensatory of the cost of the work, of which the government got the benefit." The recovery was received in 1920 and the Supreme Court held that it constituted gross income for that year despite the fact that in the prior years the taxpayer had suffered net losses in the conduct of its business which were in some measure attributable to expenditures made to produce the net income of the latter period. In so holding the Court pointed out that there was no statutory authority for disregarding the annual accounting periods to permit the bringing forward of losses sustained in the prior years to offset the taxable income received in a later year. The Court found, however, that the money received in the later year was in the nature of an income item, as distinguished [fol. 19] from a non-income item such as a return of capital. On that point the Court said:

That the recovery by respondent in 1920 was gross income for that year within the meaning of these sections

cannot, we think, be doubted. The money received was derived from a contract entered into in the course of respondent's business operations for profit. While it equalled, and in a loose sense was a return of, expenditures made in performing the contract, still as the Board of Tax Appeals found, the expenditures were made in defraying the expenses incurred in the prosecution of the work under the contract for the purpose of earning profits. They were not capital investments, the cost of which, if converted, must first be restored from the proceeds before there is a capital gain taxable as income. See Doyle v. Mitchell Brothers Co., supra, page 185 of 247 U. S. 38 S. Ct. 467.

In cases involving bad debts, which are similar to the instant case in that the original disbursement represents an outlay of capital, we have held that, where a bad debt deduction does not effect an offset of taxable income for the years deducted, then a recovery of the debt in a subsequent year should not be included in gross income in the year of recovery. State-Planters Bank & Trust Co., 45 B. T. A. 630, and National Bank of Commerce of Seattle, 40 B. T. A. 72; affd., 115 Fed. (2d) 875. In the last case we also said that, where the amount previously deducted effects an offset of taxable income, the subsequent recovery should be included in taxable income. The reason behind the ruling is that by the prior deduction of the amount of the loss from taxable income the taxpayer has already had, for income tax purposes, a recoupment of the capital out of taxable income. Any further recovery is accordingly in the nature of a replacement of taxable income and, being in excess of the reduced cost of the capital asset, is equivalent to gain to the taxpayer. Affirming National Bank of Commerce of Seattle, the court stated the principle as follows:

* * * when * * * * a loan becomes worthless, the amount thereof is loss of capital, but the income tax laws permit the bank to recoup its capital by deducting from the profits or income the amount of the loss. Thus the bank does not pay a tax on all its income, but on the amount of income less the loss on the worthless debt. The debt itself then loses its nature as capital, but represents that portion of the income which was not taxed, and the capital is the money taken from the profits or income. If the loan, after being deducted from income, is paid, then the lender is receiving profit or income—otherwise the lender would

doubt its capital on one transaction. In other words the profits or income used to pay back the capital when the debt is charged off is represented by the worthless loan, so that when such loan is paid the profits are replaced.

Applying the rationale of that case to the facts in the instant case, we conclude that, since the deductions taken by the decedent in 1930 and 1931 did not effect an offset of taxable income, the recovery in 1939 must be treated as a return of capital rather than taxable income. This conclusion is in accord with the principle expressed in Central Loan & Investment Co., 39 B. T. A. 981, and Amsco-Wire [fol. 20] Products Corporation, 44 B. T. A. 717. The respondent's argument seems to be that those cases have been erroneously decided, but he cites no authority to the contrary. In fact, as pointed out in Central Loan & Investment Co., supra, and National Bank of Commerce of Seattle, supra, the conclusions reached therein are in accord with the views expressed by the General Counsel of the Bureau of Internal Revenue in G. C. M. 18525 (C. B. 1937–1, p. 80) and G. C. M. 20854 (C. B. 1939–1, p. 102). The rulings expressed therein were in effect during the taxable year, but have since been modified or revoked by G. C. M. 22163 (C. B. 1940–2, p. 76). Our conclusion here also seems to be in accord with the recent case of Seldon R. Glenn *v.* Louisville Trust Co.—Fed. (2d)—(C. C. A., 6th Cir., Jan. 6, 1942).

In view of our holding that the net recovery of $29,750.63 received by the decedent in 1939 does not constitute income, it is unnecessary to consider petitioner's alternative contention that if the recovery constitutes income it should be taxed as capital gain.

Petitioner concedes an affirmative issue raised in the respondent's amended answer relating to the deduction of certain business expenses.

Decision will be entered under Rule 50.

UNITED STATES BOARD OF TAX APPEALS, WASHINGTON

Docket No. 106566

ESTATE OF JAMES N. COLLINS, DECEASED, FIRST NATIONAL BANK AND TRUST COMPANY OF MINNEAPOLIS, EXECUTOR, Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent.

DECISION

Pursuant to the Opinion of the Board promulgated March 27, 1942, the parties herein having filed on April 22, 1942, an agreed recomputation of tax in accordance therewith, it is

Ordered and decided: That there is no deficiency in income tax for the year 1939.

Enter:

(Signed) Arthur J. Mellett, Member.

Entered Apr. 25, 1942.

[fol. 21] UNITED STATES BOARD OF TAX APPEALS

Docket No. 106566

ESTATE OF JAMES N. COLLINS, DECEASED, FIRST NATIONAL BANK AND TRUST COMPANY OF MINNEAPOLIS, EXECUTOR, Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent.

U. S. Board of Tax Appeals, filed at hearing June 18, 1941

STIPULATION OF FACTS

It is hereby stipulated and agreed by and between the parties hereto, by their respective counsel, that the following facts shall be taken as true, provided, however, (1) that each of the parties hereto reserves the right to object to the admissibility in evidence of any of such facts on the ground of irrelevancy and immateriality and (2) that this stipulation shall be without prejudice to the right of either party to introduce other and further evidence not inconsistent herewith:

I

James N. Collins, a resident of Hennepin County, Minnesota, filed, within the time required by law, his 1939 Federal income tax return with the Collector of Internal Revenue at St. Paul, Minnesota. Said James N. Collins died on April 21, 1941, and First National Bank and Trust Company of Minneapolis, petitioner herein, is the duly appointed, authorized, and acting Executor under the Will of said James N. Collins.

II

In 1929 decedent purchased at various times in transactions entered into for profit a total of 300 shares of capital stock of National City Bank (hereinafter referred to as the stock), the purchases carrying with them at no additional cost proportionate beneficial interests in the stock of National City Company (of New York). In 1933 the name of the latter company was changed to City Company of New York. These purchases were made by decedent in the State of Minnesota from the National City Company.

III

In 1930 the decedent sold 100 shares of said stock, together with said beneficial interests in the capital stock of National City Company, which had cost him $56,200 for $14,599.20, [fol. 22] thereby sustaining a deductible loss for Federal income tax purposes in the amount of $41,600.80. This loss, which the decedent claimed as a deduction from gross income in his Federal income tax return for 1930, was allowed as a deduction by the Respondent.

IV

In 1931 the decedent sold 100 shares of said stock, together with said beneficial interests in the capital stock of National City Company, which had cost him $37,100 for $8,936.22, thereby sustaining a deductible loss for Federal income tax purposes in the amount of $28,163.78. This loss was claimed by decedent as a deduction from gross income in his Federal income tax return for 1931 and the loss was allowed as a deduction by the Respondent.

V

The remaining 100 shares of the stock referred to in paragraph III, supra, which cost the decedent $30,000, has never

been disposed of but was held and owned by the decedent up until the time of his death and is now held and owned by the Petitioner.

VI

Until the fall of 1936 decedent regarded the aforesaid purchases and sales as closed and completed transactions. During the fall of 1936 decedent learned for the first time that said stock had not been registered in accordance with the requirements of the Minnesota Blue Sky laws and for the first time decedent learned of facts which led him to believe that said sales might have been fraudulent. On August 23, 1937, the decedent filed a suit against National City Company in an effort to recover the amounts which he paid for the stock in 1929. The decedent's contentions in said action were (1) that the stock had been sold to him without having been registered in accordance with the requirements of the Minnesota Blue Sky laws and (2) that the sales had been fraudulent. A copy of the complaint in said action is attached hereto, marked Exhibit A, and made a part hereof the same as if fully set forth herein.

VII

This suit was settled by the payment to the decedent in 1939 of $67,725.95, representing 84% of $80,626.13, which amount represented the loss sustained by decedent on his dealings in National City Bank stock with National City Company. Said loss does not correspond with the figures set forth above because all of the losses sustained by de- [fol. 23] cedent were not involved in said litigation with National City Company. On March 28, 1939, said action was dismissed with prejudice pursuant to stipulation between the parties thereto. A copy of the stipulation for dismissal executed on such settlement is attached hereto, marked Exhibit B, and made a part hereof the same as if fully set forth herein.

VIII

The amount received by the decedent on account of the aforesaid settlement, after deducting attorneys' fees and other expenses in connection with the suit, was $45,150.63. Of said total net recovery $29,750.63 is allocable to the stock sold by the decedent in 1930 and 1931 (see paragraphs III and IV, supra). Of said amount of $29,750.63, $23,296.45

is allocable to the stock sold by decedent in 1930 and the balance, or $6,454.18, is allocable to the stock sold by the decedent in 1931.

IX

In his Federal income tax return for 1939 the decedent reported no income as the result of the receipt of said $29,750.63. In the deficiency notice from which the appeal herein was taken the Respondent adjusted the amount of income reported by the decedent by adding thereto said $29,750.63, thus treating the entire amount of said net recovery as gross income to the Petitioner taxable in full. The Respondent did not add the amount of said net recovery with respect to the 100 shares of stock referred to in paragraph V, supra, which was not disposed of by the decedent and which is still held and owned by the Petitioner. It is conceded that the recovery allocable to the latter stock does not constitute taxable income.

X

If the entire deduction of $41,600.80, which was claimed and allowed on decedent's 1930 Federal income tax return (paragraph III hereof), had been disallowed, no deficiency in decedent's Federal income tax liability for 1930 would have resulted, as shown by the following computation:

Net income per return	($65,896.51)
Add loss claimed on sale of National City Bank stock with respect to which James N. Collins made a recovery in 1939	41,600.80
Net income revised	($24,295.71)
Total tax assessable	None

Throughout 1939 adjustment of decedent's Federal income tax liability for 1930 was barred by the statute of limitations.

[fol. 24]

XI

If decedent had received $23,296.45 on the sale of the stock in 1930 in addition to the amounts received upon the sale of the stock as set forth in paragraph III hereof, his 1930

loss would have been $42,600.06 and his Federal income tax liability for 1930 would have been zero, computed as follows:

Net income as shown in the original return	($65,896.51)
Add: Entire amount recovered in 1939 in reduction of loss on stock sold in 1930	23,296.45
Net income revised	($42,600.06)
Total tax assessable	None

XII

If the entire deduction of $28,163.78, which was claimed and allowed on decedent's 1931 Federal income tax return (paragraph IV hereof), had been disallowed, no deficiency in decedent's Federal income tax liability for 1931 would have resulted, as shown by the following computation:

Net income per return	($40,204.90)
Add loss claimed on sale of National City Bank stock with respect to which James N. Collins made recovery in 1939	28,163.78
Net income devised	($12,041.12)
Total tax assessable	None

Throughout 1939 adjustment of decedent's Federal income tax liability for 1931 was barred by the statute of limitations.

XIII

If decedent had received $6,454.18 on the sale of the stock in 1931 in addition to the amounts received upon the sale of the stock as set forth in paragraph IV hereof, his 1931 loss would have been $33,750.72 and his Federal income tax liability for 1931 would have been zero, computed as follows:

Net income as shown in original return	($40,204.90)
Add entire amount recovered in 1939 in reduction of loss on stock sold in 1931	6,454.18
Net income revised	(33,750.72)
Total tax assessable	None

XIV

Photostats of decedent's Federal income tax returns for the years 1930, 1931, and 1939 are attached hereto, marked Exhibits C, D, and E, respectively, and made a part hereof as if fully set forth herein. The income, deductions, and credits for the years 1930 and 1931 set forth in said returns are true and correct and Respondent has made no change [fol. 25] therein upon audit of said returns.

XV

Petitioner concedes the affirmative issue raised in the Respondent's amended answer.

John W. Windhorst, Counsel for Petitioner.

(Signed) J. P. Wenchel, D. A. T., Chief Counsel, Bureau of Internal Revenue, Counsel for Respondent.

United States Circuit Court of Appeals for the Eighth Circuit

B. T. A. Docket No. 106566

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, Petitioner on Review

vs.

ESTATE OF JAMES N. COLLINS, DECEASED, FIRST NATIONAL BANK AND TRUST COMPANY OF MINNEAPOLIS, EXECUTOR, Respondent on Review

Received July 14, 1942. U. S. Board of Tax Appeals.

PETITION FOR REVIEW

To the Honorable Judges of the United States Circuit Court of Appeals for the Eighth Circuit:

Guy T. Helvering, Commissioner of Internal Revenue, holding office by virtue of the laws of the United States, hereby petitions for review by the United States Circuit Court of Appeals for the Eighth Circuit of the decision entered by the United States Board of Tax Appeals on April 25, 1942, ordering and deciding that there is no deficiency in income tax for the year 1939 due from the taxpayer, First National Bank and Trust Company of Minneapolis, Executor, Estate of James N. Collins, Deceased, the

respondent on review: The income tax return for the year 1939 was filed with the Collector of Internal Revenue for the District of Minnesota, located at St. Paul, Minnesota.

[fol. 26] The question presented is whether the decedent received income in the amount of $29,750.63 which is an allocable portion of the sum of $67,725.95 received by him in 1939 in compromise of a suit filed against the National City Company of New York for rescission of a contract entered into in 1929 for the purchase of bank stock. The decedent sold part of the stock in 1930 and 1931 at losses which he claimed as deductions in his income tax returns for these years. Until the fall of 1936 the decedent regarded the purchase and sales of the stock as closed and completed transactions, but upon learning that the stock had not been registered under the Massachusetts Blue Sky Laws, subsequently instituted the suit which led to the recovery in 1939. The decedent did not report as taxable income any part of the amount recovered by him and the Commissioner included in taxable income the sum of $29,750.63, the part allocable to the stock sold in 1930 and 1931, as taxable income in the deficiency notice issued by him.

The Board of Tax Appeals reversed the Commissioner's determination and held that no part of the sum $29,750.63, allocable to the stock sold by the decedent in 1930 and 1931, is includible in taxable income for 1939 for the reason that the decedent did not derive a tax benefit from the deductions for the losses taken in 1930 and 1931.

The Commissioner avers that in the record and proceedings before the United States Board of Tax Appeals and in the opinion and decision rendered and entered by the United States Board of Tax Appeals manifest error occurred and intervened to the prejudice of the Commissioner who now assigns the following points on which he intends to rely in this proceeding:

The United States Board of Tax Appeals erred—

(1) In holding and deciding that no part of $29,750.63 recovered by the decedent in 1939 in settlement of a suit for rescission of a contract for the purchase of stock in 1929, part of which stock was sold in 1930 and 1931 and losses therefrom were claimed and allowed as deductions from gross income in determining the income tax liability of the decedent for the years 1930 and 1931, should be included in the decedent's gross income for 1939.

(2) In failing to hold and decide that $29,750.63 of the amount recovered by the decedent in 1939 in settlement of a suit for rescission of a contract for the purchase of bank stock in 1929, part of which stock was sold in 1930 and 1931 and losses therefrom were claimed and allowed as deductions from gross income in determining the income tax liability of the decedent for the years 1930 and 1931, constituted taxable income for 1939.

[fol. 27] (3) In entering its decision wherein it ordered and decided that there is no deficiency in income tax due for the calendar year 1939.

(4) In failing and refusing to enter its decision redetermining that there is a deficiency in income tax in the amount of $2,644.58 for the taxable year 1939.

(5) In that its decision is not supported by the evidence.

(6) In that its decision is contrary to law and regulations.

(Sgd.) Samuel O. Clark, Jr., Assistant Attorney General; (Signed) J. P. Wenchel, R. L. W., Chief Counsel, Bureau of Internal Revenue, Attorneys for Petitioner on Review.

RHT/mer 6/25/42.

UNITED STATES CIRCUIT COURT OF APPEALS FOR THE EIGHTH CIRCUIT

B. T. A. Docket No. 106566

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, Petitioner on Review

vs.

ESTATE OF JAMES N. COLLINS, DECEASED, FIRST NATIONAL BANK AND TRUST COMPANY OF MINNEAPOLIS, EXECUTOR, Respondent on Review

Received July 21, 1942. U. S. Board of Tax Appeals.

NOTICE OF FILING PETITION FOR REVIEW

To First National Bank and Trust Company of Minneapolis, Executor, Estate of James N. Collins, Deceased, Minneapolis, Minnesota.

You are hereby notified that the Commissioner of Internal Revenue did, on the 14th day of July, 1942, file with the

United States Board of Tax Appeals, at Washington, D. C., a petition for review by the United States Circuit Court of Appeals for the Eighth Circuit of the decision of the Board [fol. 28] heretofore rendered in the above-entitled case. A copy of the petition for review as filed is hereto attached and served upon you.

Dated this 14th day of July 1942.

(Signed) J. P. Wenchel, R. L. W., Chief Counsel, Bureau of Internal Revenue.

Personal service of the above and foregoing notice, together with a copy of the petition for review mentioned therein is hereby acknowledged this — day of July 1942.

(S.) First National Bank and Trust Co., Minneapolis, Minn. L. A. Lyson, Assistant Secretary, Respondent on Review.

RHT/mer 6/25/42.

UNITED STATES CIRCUIT COURT OF APPEALS FOR THE EIGHTH CIRCUIT

B. T. A. Docket No. 106566

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, Petitioner on Review

vs.

ESTATE OF JAMES N. COLLINS, DECEASED, FIRST NATIONAL BANK AND TRUST COMPANY OF MINNEAPOLIS, EXECUTOR, Respondent on Review

Received Aug. 21, 1942. U. S. Board of Tax Appeals.

PRAECIPE FOR RECORD

To the Clerk of the United States Board of Tax Appeals:

You will please prepare, transmit and deliver to the Clerk of the United States Circuit Court of Appeals for the Eighth Circuit, copies duly certified as correct of the following documents and records in the above-entitled cause in connection with the petition for review by the said Circuit Court of Appeals for the Eighth Circuit, heretofore filed by the Commissioner of Internal Revenue:

1. Docket entries of the proceedings before the Board.

[fol. 29] 2. Pleadings before the Board: (a) Petition, including annexed copy of deficiency letter; (b) Answer.

3. Findings of fact, opinion and decision of the Board.

4. Petition for review, together with proof of service of notice of filing petition for review and of service of a copy of petition for review.

5. Orders enlarging time for the preparation of the evidence and for the transmission and delivery of the record not included in record.

6. This praecipe.

(Signed) J. P. Wenchel, R. L. W., Chief Counsel, Bureau of Internal Revenue.

Service of a copy of the within praecipe is hereby admitted this 18th day of August 1942.

(S.) Leland W. Scott, Attorney for Respondent on Review.

(S.) John W. Windhorst, Attorney for Respondent on Review.

UNITED STATES BOARD OF TAX APPEALS, WASHINGTON

Docket No. 106566

COMMISSIONER OF INTERNAL REVENUE, Petitioner

v.

ESTATE OF JAMES N. COLLINS, DECEASED, FIRST NATIONAL BANK AND TRUST COMPANY OF MINNEAPOLIS, EXECUTOR, Respondent

CERTIFICATE

I, B. D. Gamble, clerk of the U. S. Board of Tax Appeals, do hereby certify that the foregoing pages, 1 to 71, inclusive, contain and are a true copy of the transcript of record, papers, and proceedings on file and of record in my office as called for by the Praecipe in the appeal (or appeals) as above numbered and entitled.

In testimony whereof, I hereunto set my hand and affix the seal of the United States Board of Tax Appeals, at Washington, in the District of Columbia, this 29 day of September 1942.

[Seal.] B. D. Gamble, Clerk, United States Board of Tax Appeals.

[fol. 30] UNITED STATES BOARD OF TAX APPEALS

Docket No. 106567

COMMISSIONER OF INTERNAL REVENUE, Petitioner

v.

E. W. DOBSON, Respondent

ORDER ENLARGING TIME

On motion of counsel for the petitioner, it is ordered that the time for preparation, transmission and delivery of the record *sur* petition for review of the above entitled proceeding in the United States Circuit Court of Appeals, Eighth Circuit, is extended to September 19, 1942.

(Signed) J. E. Murdock, Member.

Dated: Wash. D. C., July 20, 1942.
lj.

Now, Sept. 2, 1942 the foregoing order is certified from the record as a true copy.

B. D. Gamble, Clerk, U. S. Board of Tax Appeals.

[Endorsed:] Filed in U. S. Circuit Court of Appeals on Sept. 4, 1942.

BEFORE UNITED STATES BOARD OF TAX APPEALS

Docket No. 106567

E. W. DOBSON, Petitioner

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent

Appearances: For Taxpayer: Leland W. Scott, Esq., John W. Windhorst, Esq. For Comm'r.: S. U. Hiken, Esq.

DOCKET ENTRIES

1941

Mar. 3—Petition received and filed. Taxpayer notified. Fee paid.

Mar. 3—Copy of petition served on General Counsel.

Mar. 3—Request for Circuit hearing in St. Paul, Minnesota, filed by taxpayer. 3/3/41 copy served.

Mar. 31—Answer filed by General Counsel.

[fol. 31] Apr. 3—Copy of answer served on taxpayer. (St. Paul, Minnesota.)

Apr. 28—Hearing set June 16, 1941, St. Paul, Minnesota.
June 18—Hearing had before Mr. Turner on the merits submitted. Stipulation as to the facts. Briefs due Aug. 2, 1941. Reply briefs Aug. 18, 1941.
July 25—Brief filed by taxpayer.
July 28—Motion for extension to Aug. 15, 1941, to file brief filed by General Counsel. 7/31/41 granted.
Aug. 2—Transcript of hearing 6/18/41 filed.
Aug. 11—Motion for extension of time to Aug. 30, 1941, to file brief filed by General Counsel. 8/14/41 granted.
Aug. 29—Brief filed by General Counsel.
Sept. 2—Copy of brief served on General Counsel.
Sept. 13—Reply brief filed by taxpayer. 9/15/41 copy served.

1942

Mar. 30—Memorandum opinion rendered. Turner, Decision will be entered for petitioner. 3/30/42 copy served.
Mar. 30—Decision entered. Murdock, Div. 3.
June 22—Petition for review by U. S. Circuit Court of Appeals, 8th Circuit, with assignments of error filed by General Counsel.
June 30—Affidavit of service filed.
July 1—Proof of service of petition for review filed.
July 20—Motion for extension to 9/21/42 to transmit record filed by General Counsel.
July 20—Order enlarging time to Sept. 19, 1942, to prepare and deliver the record entered.
Aug. 21—Praecipe for record filed by General Counsel, with proof of service thereon.

UNITED STATES BOARD OF TAX APPEALS

Docket No. 106567

E. W. DOBSON, Petitioner

vs.

COMMISSIONER OF INTERNAL REVENUE, Respondent

Received Mar. 3, 1941. U. S. Board of Tax Appeals.

PETITION

The above named Petitioner hereby petitions for a redetermination of the deficiency set forth by the Commis-

[fol. 32] sioner of Internal Revenue in his Notice of Deficiency dated January 11, 1941, and as a basis for the proceeding alleges:

I

The Petitioner, E. W. Dodson, is an individual residing in the City of Wayzata, County of Hennepin, State of Minnesota. On or about March 15, 1940, Petitioner filed an income tax return for the calendar year 1939 with the Collector of Internal Revenue of the United States in and for the District of Minnesota.

II

The Notice of Deficiency, a copy of which, marked Exhibit A, is attached hereto and hereby made a part hereof, was mailed to Petitioner on January 11, 1941. The taxes in controversy are income taxes for the calendar year 1939 asserted against the Petitioner by said notice.

III

The Notice of Deficiency determined that Petitioner's income tax liability for the calendar year 1939 was $8,823.75. Of this amount $1,332.89 was paid by the Petitioner during the calendar year 1940 and Respondent determined a deficiency in Petitioner's income tax liability for the calendar year 1939 in the sum of $7,490.86. The entire amount of said deficiency is in controversy.

IV

The determination of tax set forth in said Notice of Deficiency is based on the following errors:

(a) Respondent erred in determining that the entire amount of $32,384.80, recovered by Petitioner during the calendar year 1939 from National City Company, constituted income taxable to the Petitioner.

(b) Respondent erred in determining that $31,432.80 of said $32,384.80, recovered by Petitioner from National City Company did not constitute a return of capital to the Petitioner.

(c) Respondent erred in determining that Petitioner realized income in excess of the sum of $952 as the result of the

recovery by Petitioner of said $32,384.80 from said National City Company.

(d) Respondent erred in determining that the income realized by Petitioner as the result of said recovery from National City Company did not constitute capital gain under the provisions of Section 117 of the Internal Revenue Code.

[fol. 33] (e) Respondent erred in determining that there is a deficiency in Petitioner's income tax liability for the calendar year 1939.

V

The facts upon which Petitioner relies as a basis for this proceeding are as follows:

(a) On or about the dates and for the amounts set forth below the Petitioner purchased and sold stock of National City Bank of New York:

1. On December 11, 1928, Petitioner purchased 40 shares at a cost of $10,120.

2. On April 10, 1929, Petitioner purchased 50 shares at a cost of $18,850.

3. On August 16, 1929, Petitioner purchased 70 shares at a cost of $27,580.

4. On October 10, 1929, Petitioner purchased 40 shares at a cost of $19,800.

5. On October 29, 1929, Petitioner sold the 200 shares purchased at items 1, 2, 3, and 4 above for $74,000.

6. On October 30, 1929, Petitioner purchased 200 shares at a cost of $70,000.

7. On December 3, 1930, Petitioner sold the 200 shares purchased at item 6 above for $20,697.44.

8. On July 3, 1931, Petitioner purchased 200 shares at a cost of $17,700.

9. On July 13, 1931, Petitioner sold the 200 shares purchased at item 8 above for $16,000.

The cost of the purchases described above represents the actual cash outlay of the Petitioner and does not necessarily

determine the income tax cost of said stock to the Petitioner inasmuch as some of the above sales represent wash sales of said stock, thereby increasing the cost of subsequent purchases of said stock as required by the Revenue Act of 1928.

(b) On or about March 15, 1931, the Petitioner filed with the Collector of Internal Revenue of the United States in and for the District of Minnesota an income tax return for the calendar year 1930. Said income tax return disclosed the following gross income and deductions therefrom:

Income:		
Salaries	$10,400.00	
Dividends on stock of domestic corporations	13,130.60	
Total income		$23,530.60
[fol. 34] Deductions:		
Interest paid	$4,425.60	
Loss on sale of stock of National City Bank of New York	49,302.50	
Total deductions		53,728.16
Net income		None

Except as hereinafter set forth with respect to the loss arising from the sale of stock of National City Bank of New York, the income and deductions set forth above are a true and correct statement of Petitioner's net income for the calendar year 1930 and Respondent has not made any changes therein. The loss sustained on the sale of stock of National City Bank of New York in the sum of $49,302.50, described in said return, was realized from the sale of 200 shares of said stock for the sum of $20,697.44 on December 3, 1930, as set forth at item V (a) 7 above. In Petitioner's income tax return for said calendar year 1930 the cost of said stock was set forth as $70,000. The correct income tax cost of said stock was $77,000 and the Petitioner therefore sustained a loss upon the sale of said stock in 1930 in the sum of $57,673.94.

(c) During the calendar year 1939 the Petitioner instituted suit against the National City Company for the re-

covery of the purchase price of stock of National City Bank of New York purchased from said National City Company on April 10, 1929, August 16, 1929, October 10, 1929, and October 30, 1929, as set forth in paragraph V (a) 2, 3, 4, 6, and 8 above. Said suit was dismissed and Petitioner received as consideration for said dismissal the net amount of $32,384.80. The sum of $31,432.80 was recovered with respect to the 50 shares of stock purchased on April 10, 1929 (item V (a) 2 above), the 70 shares of stock purchased on August 16, 1929 (item V (a) 3 above), the 40 shares of stock purchased on October 10, 1929 (item V (a) above), and the 200 shares of stock purchased on October 30, 1929 (item V (a) 6 above); and $952 was recovered with respect to the $200 shares of stock purchased on July 3, 1931 (item V (a) 8 above).

(d) Except for said recovery of $32,384.80 during the calendar year 1939 Petitioner has not been reimbursed in any manner for the loss sustained on the sale of stock of National City Bank of New York as set forth in paragraph V (a) above.

Wherefore, Petitioner prays that this Board may hear the proceeding and decide that:

(a) Respondent erred in determining that the entire amount of $32,384.80, recovered by Petitioner during the calendar year 1939 from National City Company, constituted income taxable to the Petitioner.

[fol. 35] (b) Respondent erred in determining that $31,432.80 of said $32.384.80 recovered by Petitioner from National City Company did not constitute a return of capital to the Petitioner.

(c) Respondent erred in determining that Petitioner realized income in excess of the sum of $952 as the result of the recovery by Petitioner of said $32,384.80 from said National City Company.

(d) Respondent erred in determining that the income realized by Petitioner as the result of said recovery from National City Company did not constitute capital gain under the provisions of Section 117 of the Internal Revenue Code.

(e) Respondent erred in determining that there is a deficiency in Petitioner's income tax liability for the calendar year 1939.

Leland W. Scott, John W. Windhorst, 1300 First National-Soo Line Bldg., Minneapolis, Minnesota, Attorneys for Petitioner.

* * * * * * *

Duly sworn to by E. W. Dobson. Jurat omitted in printing.

[fol. 36] EXHIBIT "A" TO PETITION

Form 1230 SN-IT-1

Office of Internal Revenue Agent in Charge, St. Paul Division, 800 Post Office Building.

Treasury Department, Internal Revenue Service, St. Paul, Minnesota, Jan. 11, 1941.

Collection District: Minnesota

Mr. E. W. Dodson, Wayzata, Minnesota.

SIR:

You are advised that the determination of your income tax liability for the taxable year(x) 1939 discloses a deficiency of $7,490.86 as shown in the statement attached.

In accordance with the provisions of existing internal revenue laws, notice is hereby given of the deficiency mentioned.

Within 90 days (not counting Sunday or a legal holiday in the District of Columbia as the 90th day) from the date of the mailing of this letter, you may file a petition with the United States Board of Tax Appeals for a redetermination of the deficiency.

Should you not desire to file a petition, you are requested to execute the enclosed form and forward it to the Internal Revenue Agent in Charge, St. Paul, Minnesota, for the attention of LGE-90D. The signing and filing of this form will expedite the closing of your return(s) by permitting an early assessment of the deficiency, and will prevent the accumulation of interest, since the interest period termi-

nates 30 days after filing the form, or on the date assessment is made, whichever is earlier.

Respectfully, Guy T. Helvering, Commissioner, by C. W. Rink, Internal Revenue Agent in Charge.

Enclosures: Statement. Form of Waiver.

LGE/Mrr.
GPO 2-17679.

[fol. 37] STATEMENT

Mr. E. W. Dobson, Wayzata, Minnesota

Tax Liability for Taxable Year Ended December 31, 1939

Income tax: Liability $8,823.75; assessed $1,332.89; deficiency, $7,490.86.

In making this determination of your income tax liability, careful consideration has been given to the report of examination dated November 5, 1940.

Adjustments to Net Income

Net income as disclosed by return	$17,010.67
Unallowable deductions and additional income:	
(a) Settlement income	31,432.80
Net income adjusted	$48,443.47

Explanation of Adjustments

(a) During the year 1929 you purchased 360 shares of stock of National City Bank which was sold in 1929 and 1930 at a loss. During 1939, $32,384.80 was received in settlement of a suit brought against the National City Company, based on the contention that the original sale of this stock was illegal, being in violation of the security laws of the State of Minnesota, governing such sales. It is held that the net amount received in settlement is taxable in its entirety.

Net amount received	$32,384.80
Reported	952.00
Adjustment	31,432.80

Computation of Tax

Adjusted net income	$48,443.47
Less: Personal exemption	1,250.00
Balance (surtax net income)	47,193.47
Less: Earned income credit—maximum	1,400.00
Balance subject to normal tax	45,793.47
Normal tax at 4%	1,831.74
Surtax on $47,193.47	6,942.24
Total tax	8,773.98
Total tax (alternative tax in case of a net long-term loss)	8,823.75
Total tax assessable	8,823.75
Tax previously assessed: Acct. No. 201834	1,332.89
Deficiency of income tax	7,490.86

[fol. 38] Computation of Alternative Tax

Net income adjusted	$48,443.47
Net long-term capital loss	3,240.75
Ordinary net income	51,684.22
Less: Personal exemption	1,250.00
Balance (surtax net income)	50,434.22
Less: Earned income credit	1,400.00
	49,034.22
Normal tax at 4% on $49,034.22	1,961.37
Surtax on $50,434.22	7,834.61
Total partial tax	9,795.98
30% of net long-term capital loss	972.23
Total alternative tax	8,823.75

UNITED STATES BOARD OF TAX APPEALS

Docket No. 106567

E. W. DOBSON, Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent

Received Mar. 31, 1941. U. S. Board of Tax Appeals.

ANSWER

Now comes the Commissioner of Internal Revenue, by his attorney, J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue, and for answer to the petition filed herein admits, denies, and alleges as follows:

I and II. Admits the allegations contained in paragraphs I and II of the petition.

III. Admits that in the notice of deficiency it was determined that petitioner's income tax liability for the calendar year 1939 is $8,823.75; admits that respondent determined a deficiency in petitioner's income tax liability for the calendar year 1939 in the sum of $7,490.86; admits that the entire amount of said deficiency is in controversy; denies the remaining allegations contained in paragraph III of the petition.

IV. (a) to (e), inclusive. Denies that the respondent erred as alleged in subparagraphs (a) to (e), inclusive, of paragraph IV of the petition.

V. (a) Admits that sometime in 1929 the petitioner purchased 360 shares of stock of National City Bank; admits [fol. 39] that petitioner sold said stock at a loss in 1929 and 1930; denies the remaining allegations contained in subparagraph (a) of paragraph V of the petition.

V. (c) *Admits that during the caendar year 1929 the peti-* (b) of paragraph V of the petition, except it is admitted that in 1930 the petitioner sustained a substantial loss, the exact amount of which is unknown to the respondent, on the sale sometime in that year of National City Bank stock purchased by the petitioner in 1929.

V. (c) Admits that during the calendar year 1929 the petitioner instituted a suit against the National City Company; admits that petitioner received the net amount of $32,384.80 in 1939 on account of the institution of said suit; denies the remaining allegations contained in subparagraph (c) of paragraph V of the petition.

V. (d) Denies the allegations contained in subparagraph (d) of paragraph V of the petition.

Denies generally and specifically each and every allegation contained in the petition not hereinbefore specifically admitted, qualified or denied.

Wherefore, respondent prays that the Board redetermine the deficiency herein to be the amount determined by the Commissioner, viz: $7,490.86 in respect of income taxes for the taxable year 1939.

(Signed) J. P. Wenchel, S. U. H., Chief Counsel, Bureau of Internal Revenue.

Of Counsel: F. R. Shearer, Division Counsel; S. U. Hiken, Special Attorney, Bureau of Internal Revenue.

[fol. 40] UNITED STATES BOARD OF TAX APPEALS

Docket No. 106567

E. W. DOBSON, Petitioner

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent

John W. Windhorst, Esq., and Leland W. Scott, Esq., for the petitioner.

S. U. Hiken, Esq., for the respondent.

MEMORANDUM OPINION

TURNER: The respondent determined a deficiency in income tax for the year 1939 in the amount of $7,490.86. The issue presented is whether a sum of money, or any part thereof, recovered by the petitioner in the taxable year as a result of litigation involving certain stock transactions in prior years constitutes a return of capital, as contended by petitioner, or taxable income, as contended by the respondent. The parties have filed a written stipulation of facts

with certain exhibits attached and the Board adopts such stipulation as its findings of fact. We shall recite only the facts deemed necessary to discussion of the issue presented.

Petitioner, a resident of Wayzata, Minnesota, filed his 1939 income tax return with the collector of internal revenue at St. Paul, Minnesota.

At various times in 1928, 1929, and 1931 the petitioner purchased, in transactions entered into for profit, a total of 600 shares of the capital stock of the National City Bank of New York. The stock also carried certain beneficial interests in the stock of the National City Company of New York. The purchases were made in the State of Minnesota from the National City Company.

In 1929 the petitioner sold 200 shares of the stock which had cost him $76,350 for $74,000, thereby sustaining a loss of $2,350. This loss was not claimed as a deduction by the petitioner in his 1929 income tax return because of the wash-sales provisions of the Revenue Act of 1928, and it would not have been allowed if it had been claimed.

In 1930 petitioner sold 200 shares of the stock which had cost him $70,000 for $20,697.44, thereby sustaining a loss in the amount of $49,302.56, which loss was claimed as a deduction in his return for 1930. Although the deductible loss [fol. 41] actually sustained on this sale was $2,350 greater than that claimed by the petitioner in his return, because of the increased basis resulting from the 1929 wash-sale, the deduction actually claimed by petitioner in his return of 1930 was not disturbed by the respondent because the return showed a net loss.

In 1931 the petitioner sold the remaining 200 shares of the stock which had cost him $17,700 for $16,000 thereby sustaining a deductible loss for income tax purposes in the amount of $1,700. This loss was claimed by petitioner as a deduction from gross income in his return for 1931 and was allowed as a deduction by the respondent.

Until September 1937 the petitioner regarded the aforesaid purchases and sales as closed and completed transactions. During that month petitioner learned for the first time that the stock had not been registered under the Minnesota Blue Sky laws, and further learned for the first time facts which led him to believe that the sales by the company to him might have been fraudulent. On July 9, 1938 he filed a suit against National City Company in an effort to recover the amounts which he had paid for the stock in

1928, 1929 and 1931, alleging that the stock had been sold to him without having been registered in accordance with the requirements of the Minnesota Blue Sky laws and that the sales had been fraudulent. He asked for a rescission of the entire transaction and tendered to the defendant company the proceeds of the stock or an equivalent number of shares of stock of the bank, plus interest and dividends received.

In 1939 the suit was settled by a net payment of $32,384.80 by the company to the petitioner, and upon receipt thereof the suit was dismissed with prejudice pursuant to a stipulation between the parties. Of the total net recovery $31,432.80 is allocable to the stock sold by petitioner in 1930 and the balance of $952 is allocable to the stock sold by petitioner in 1931. It is conceded that the last amount mentioned constituted taxable income to the petitioner for the year 1939 and was reported as income in his return for that year.

Of the deduction of $49,302.56 which was claimed and allowed on petitioner's 1930 income tax return, $5,983.51 thereof is attributable to 40 shares of stock which had been purchased by petitioner in 1928 and none of the recovery by petitioner in 1939 was attributable to such loss. If the balance of the deduction, $43,319.05, had been disallowed no deficiency in petitioner's income tax liability for 1930 would have resulted, as shown by the following computation:

[fol. 42] Net loss per return		($30,197.56)
Add loss claimed on sale of National City Bank stock with respect to which Petitioner made a recovery in 1939		43,319.05
Net income revised		13,121.49
Less:		
Dividends	$13,130.60	
Personal exemption	00.00	
Credit for dependents	00.00	
Total		13,130.60
Balance subject to normal tax		None
Normal tax: 1½% on first $4,000		None
Surtax on $13,121.49		31.21
Less earned income credit		39.25
Total tax assessable		None

If the petitioner had received $31,432.80 on the sale of the stock in 1930 in addition to the amount actually received on such sale, the said $31,432.80 being the amount actually recovered in respect of such stock by reason of the settlement in 1939, his 1930 loss on the sale of the stock would have been $20,219.76, and he would have had no income tax liability for that year, as shown by the following computation:

Net income as shown in original return		($30,197.56)
Add: Entire amount recovered in 1939 in reduction of loss on stock sold in 1930		31,432.80
Net income revised		1,235.24
Less:		
Dividends	$13,130.60	
Personal exemption	00.00	
Total		13,130.60
Balance subject to normal tax		None
Total tax assessable		None
Tax assessed		None
Deficiency		None

Throughout the year 1939 adjustment of petitioner's income tax liability for 1930 was barred by the statute of limitations.

In his income tax return for 1939 the petitioner reported income of only $952 on account of the recovery of $32,384.80. In the deficiency notice the respondent adjusted the amount of gross income reported by adding thereto $31,432.80, thereby treating the entire amount of petitioner's net recovery of $32,384.80 as gross income.

Petitioner contends that the suit brought by him against the National City Company was in the nature of an action for rescission of the original contract and that the amount recovered in 1939 is in the nature of a capital recovery which [fol. 43] does not constitute taxable income in the absence of realization of gain, either actual or constructive, and that he realized no gain since the deduction claimed in the year the stock was sold did not result in any "tax benefit" to him. In the alternative, petitioner contends that if the amount recovered is taxable to him, it is taxable as capital

gain. The respondent contends that the entire amount recovered by the petitioner from the company is taxable as ordinary gain and that it is wholly immaterial whether he realized any "tax benefit" from the deduction taken in the prior year, but that in any event, he did realize a "tax benefit" to the extent that the deduction taken in the prior year offset taxable income.

We have considered this same question in the case of Estate of James N. Collins, 46 B. T. A.—(March 27, 1942), and in that case was held that since the deduction taken by the taxpayer in the prior year did not effect an offset of taxable income, the subsequent recovery in the taxable year did not constitute taxable income. In the instant case the record shows that in 1930 petitioner claimed a loss deduction on account of the transaction in the amount of $49,302.56, and after taking such deduction his return showed a net loss of $30,197.56, and further, that the loss actually sustained by petitioner on the transaction was $2,350 greater than that claimed. Had that additional sum been claimed as a deduction, his return would have shown a net loss of $32,547.56. Therefore, to that extent the loss sustained upon the sale of the stock in the prior year did not effect an offset of taxable income, and since his recovery of $31,432.80 in the taxable year is less than said loss we hold that no part thereof constitutes taxable income. Cf. John V. Dobson, 46 B. T. A.—(March 27, 1942).

Decision will be entered for petitioner.

Entered: March 30, 1942.

UNITED STATES BOARD OF TAX APPEALS, WASHINGTON

Docket No. 106567

E. W. DOBSON, Petitioner

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent

DECISION

Pursuant to the determination of the Board, as set forth in its Memorandum Opinion, entered March 30, 1942, it is

[fol. 44] ordered and decided that there is no deficiency in income tax for the calendar year 1939.

Enter:

Entered Mar. 30, 1942.

(Signed) J. E. Murdock, Member.

UNITED STATES BOARD OF TAX APPEALS

Docket No. 106567

E. W. DOBSON, Petitioner

vs.

COMMISSIONER OF INTERNAL REVENUE, Respondent

STIPULATION OF FACTS

It is hereby stipulated and agreed by and between the parties hereto, by their respective counsel, that the following facts shall be taken as true, provided, however, (1) that each of the parties hereto reserves the right to object to the admissibility in evidence of any such facts on the ground of irrelevancy and immateriality and (2) that this stipulation shall be without prejudice to the right of either party to introduce other and further evidence not inconsistent herewith:

I

Petitioner, a resident of Wayzata, Minnesota, filed, within the time required by law, his 1939 Federal income tax return with the Collector of Internal Revenue at St. Paul Minnesota.

II

At various times in 1928, 1929, and 1931, the Petitioner purchased, in transactions entered into for profit, a total of 600 shares of the capital stock of National City Bank (hereinafter referred to as the stock), the purchases carrying with them, at no additional cost, proportionate bene-

ficial interests in the stock of National City Company (of New York). In 1933 the name of the latter company was changed to City Company of New York, Inc. These purchases were made by the petitioner in the State of Minnesota from the National City Company.

III

In 1929 the petitioner sold 200 shares of said stock, which had cost him $76,350.00, for $74,000.00, thereby sustaining a loss of $2,350.00. This loss was not claimed by the petitioner in his 1929 Federal income tax return because of the [fol. 45] wash-sales provisions of the Revenue Act of 1928, nor would it have been allowable if it had been claimed.

IV

In 1930 Petitioner sold 200 shares of the stock, which had cost him $70,000.00, for $20,697.44, thereby sustaining a loss in the amount of $49,302.56. This is the amount of the loss which was claimed as a deduction in the petitioner's income tax return for 1930. Although for income tax purposes the deductible loss sustained on this sale was $2,350.00 greater than that claimed by the petitioner, in view of the increased basis resulting from the 1929 wash-sale, the deduction actually claimed by petitioner in his return for 1930 was not disturbed by the respondent on an examination of said return because the return showed a net loss.

V

In 1931 the petitioner sold the remaining 200 shares of said stock, which had cost him $17,700.00, for $16,000.00, thereby sustaining a deductible loss for Federal income tax purposes in the amount of $1,700.00. This loss was claimed by petitioner as a deduction from gross income in his Federal income tax return for 1931 and the loss was allowed as a deduction by the respondent.

VI

Until September 1937, the Petitioner regarded the aforesaid purchases and sales as closed and completed transactions. In September 1937, the Petitioner learned for the

first time that said stock had not been registered under the Minnesota Blue Sky laws and the Petitioner also learned for the first time of facts which led him to believe that said sales might have been fraudulent. On July 9, 1938, the Petitioner filed a suit against National City Company in an effort to recover the amounts which he paid for the stock in 1928, 1829, and 1931. The Petitioner's contentions in said action were (1) that the stock had been sold to him without having been registered in accordance with the requirements of the Minnesota Blue Sky laws and (2) that the sales had been fraudulent. A copy of the complaint in said action is attached hereto, marked Exhibit A, and made a part hereof the same as if fully set forth herein.

VII

This suit was settled by the payment to Petitioner in 1939 of $32,384.80 net after the payment by him of attorneys' fees and other similar expenses. Upon payment of said sum said action was dismissed with prejudice pursuant to a [fol. 46] stipulation between the parties thereto. A true and correct copy of said stipulation for dismissal, marked Exhibit B, is attached hereto and made a part hereof the same as if fully set forth herein. Of said total net recovery $31,432.80 is allocable to the stock sold by the petitioner in 1930 (see paragraph IV supra) and the balance, or $952.00, is allocable to the stock sold by Petitioner in 1931. It is conceded that the last mentioned amount constituted taxable income to the Petitioner for the calendar year 1939 and said amount was included as such in Petitioner's return for said year.

VIII

In his Federal income tax return for 1939 the Petitioner reported income of only $952.00 (see paragraph VII supra) on account of the receipt of said $32,384.80. In the deficiency notice from which the appeal herein was taken the Respondent adjusted the amount of the income reported by the Petitioner on said recovery by adding $31,432.80 thereto, thereby treating the entire amount of petitioner's net recovery of $32,384.80 as gross income, 100 per cent taxable.

IX

Of the deduction of $49,302.56 which was claimed and allowed on Petitioner's 1930 Federal income tax return (see paragraph IV supra) $5,983.51 thereof is attributable to 40 shares of stock which had been purchased by Petitioner in 1928 and none of the recovery by Petitioner in 1939 from National City Company was attributable to such loss. If the balance of said deduction of $49,302.56, viz, $43,319.05, had been disallowed, no deficiency in Petitioner's Federal income tax liability for 1930 would have resulted as shown by the following computation:

Net loss per return		($30,197.56)
Add loss claimed on sale of National City Bank stock with respect to which Petitioner made a recovery in 1939		43,319.05
Net income revised		$13,121.49
Less:		
Dividends	$13,130.60	
Personal exemption	00.00	
Credit for dependants	00.00	
Total		13,130.60
Balance subject to normal tax		None
Normal tax: 1½% on first $4,000		None
Surtax on $13,121.49		31.21
Total		31.21
Less earned income credit		39.25
Total tax assessable		None

[fol. 47] Throughout the year 1939 adjustment of Petitioner's Federal income tax liability for 1930 was barred by the statute of limitations.

X

If the Petitioner had received $31,432.80 on the sale of the stock in 1930 in addition to the amounts received upon the sale of the stock as set forth in paragraph IV, supra, his 1930 loss on the sale of said stock would have been $20,-

219.76 and his Federal income tax liability for 1930 would have been zero, computed as follows:

Net income as shown in original return		($30,197.56)
Add: Entire amount recovered in 1939 in reduction of loss on stock sold in 1930		31,432.80
Net income revised		1,235.24
Less:		
Dividends	$13,130.60	
Personal exemption	00.00	
Total		13,130.60
Balance subject to normal tax		None
Total tax assesable		None
Tax assessed		None
Deficiency		None

XI

Photostats of the Petitioner's Federal income tax returns for the years 1930 and 1939 are attached hereto, marked Exihibits C and D, respectively, and made a part hereof the same as if fully set forth herein. The income, deductions and credits for the year 1930, which are set forth in said return are true and correct, except that said return does not show the increased basis for computing loss on the sale of the stock in 1930 on account of the 1929 wash-sale referred to in paragraph IV, supra.

Leland W. Scott, John W. Windhorst, Counsel for Petitioner. (Signed) J. P. Wenchel, D. A. T., Chief Counsel, Bureau of Internal Revenue, Counsel for Respondent.

[fol. 48] UNITED STATES CIRCUIT COURT OF APPEALS FOR THE EIGHTH CIRCUIT

B. T. A. Docket No. 106567

GUY T. HELVERING, Commissioner of Internal Revenue, Petitioner on Review

vs.

E. W. DOBSON, Respondent on Review

PETITION FOR REVIEW

To the Honorable Judges of the United States Circuit Court of Appeals for the Eighth Circuit:

Guy T. Helvering, Commissioner of Internal Revenue, holding office by virtue of the laws of the United States, hereby petitions for review by the United States Circuit Court of Appeals for the Eighth Circuit of the decision entered by the United States Board of Tax Appeals on March 30, 1942, ordering and deciding that there is no deficiency in income tax for the year 1939 due from the taxpayer, E. W. Dobson, the respondent on review. The taxpayer's income tax return for the year 1939 was filed with the Collector of Internal Revenue for the District of Minnesota, located at St. Paul, Minnesota.

The question presented is whether the taxpayer received taxable income in the amount of $31,432.80 which is an allocable portion of the sum of $32,384.80 received by him in 1939 in compromise of a suit filed against the National City Company of New York for rescission of contracts entered into in 1928 and 1929 for the purchase of bank stock. The taxpayer sold part of the stock in 1930 at a loss which he claimed as a deduction in his income tax return for that year. Until September 1937 the taxpayer regarded the purchases and sales of the stock as closed and completed transactions, but upon learning that the stock had not been registered under the Massachusetts Blue Sky Laws, instituted the suit which led to the recovery in 1939 of the sum of $32,384.80, of which he concedes $952.00 allocable to the stock sold in 1931 constitutes taxable income. The balance of the recovery amounting to $31,432.80 was not reported as taxable income by the taxpayer and was included in

taxable income in the notice of deficiency issued by the Commissioner.

The United States Board of Tax Appeals reversed the Commissioner's determination and held that the sum of $31,432.80 is not includible in taxable income for 1939 for [fol. 49] the reason that the taxpayer did not derive a tax benefit from the deduction of the loss taken in 1930.

The Commissioner avers that in the record and proceedings before the United States Board of Tax Appeals and in the opinion and decision rendered and entered by the United States Board of Tax Appeals manifest error occurred and intervened to the prejudice of the Commissioner who now assigns the following points on which he intends to rely in this proceeding:

The United States Board of Tax Appeals erred—

(1) In holding and deciding that no part of $31,432.80 recovered by the taxpayer in 1939 in settlement of a suit for rescission of contracts for the purchase of stock in 1928 and 1929, which stock was sold in 1930 and losses therefrom were claimed and allowed as deductions from gross income in determining the income tax liability of the taxpayer for the year 1930, should be included in the taxpayer's gross income for 1939.

(2) In failing to hold and decide that $31,432.80 of the amount recovered by the taxpayer in 1939 in settlement of a suit for rescission of contracts for the purchase of bank stock in 1928 and 1929, which stock was sold in 1930 and losses therefrom were claimed and allowed as deductions from gross income in determining the income tax liability of the taxpayer for the year 1930, constituted taxable income for 1939.

(3) In entering its decision wherein it ordered and decided that there is no deficiency in income tax due from this taxpayer for the calendar year 1939.

(4) In failing and refusing to enter its decision redetermining that there is a deficiency in income tax due from the taxpayer in the amount of $7,490.86 for the taxable year 1939.

(5) In that its decision is not supported by the evidence.

(6) In that its decision is contrary to law and regulations.

Samuel O. Clark, Jr., *Assistant Attorney General*, (Signed J. P. Wenchel, R. L. W. *Chief Counsel, Bureau of Internal Revenue, Attorneys for Petitioner on Review.*

RET/mer 6/10/42.

[fol. 50] UNITED STATES CIRCUIT COURT OF APPEALS FOR THE EIGHTH CIRCUIT

B. T. A. Docket No. 106567

GUY T. HELVERING, Commissioner of Internal Revenue, Petitioner on Review

vs.

E. W. DOBSON, Respondent on Review

United States Board of Tax Appeals, July 1, 1942

NOTICE OF FILING PETITION FOR REVIEW

To Leland W. Scott, Esquire, John W. Windhorst, Esquire, 1300 First National-Soo Line Building, Minneapolis, Minnesota:

You are hereby notified that the Commissioner of Internal Revenue did, on the 22nd day of June 1942, file with the United States Board of Tax Appeals, at Washington, D. C., a petition for review by the United States Circuit Court of Appeals for the Eighth Circuit of the decision of the Board heretofore rendered in the above-entitled cause. A copy of the petition for review as filed is hereto attached and served upon you.

Dated this 22nd day of June 1942.

(S.) B. D. Gamble, Clerk, United States Board of Tax Appeals.

Personal service of the above and foregoing notice, together with a copy of the petition for review mentioned therein is hereby acknowledged this 29th day of June 1942.

(S) Leland W. Scott, Attorney for Respondent on Review (S.) John W. Windhorst, Attorney for Respondent on Review.

ENT/mer 6/10/42.

[fol. 51] UNITED STATES CIRCUIT COURT OF APPEALS FOR THE EIGHTH CIRCUIT

B. T. A. Docket No. 106567

GUY T. HELVERING, Commissioner of Internal Revenue, Petitioner on Review

vs.

E. W. DOBSON, Respondent on Review

Received Aug. 21, 1942. U. S. Board of Tax Appeals

PRAECIPE FOR RECORD

To the Clerk of the United States Board of Tax Appeals:

You will please prepare, transmit, and deliver to the Clerk of the United States Circuit Court of Appeals for the Eighth Circuit, copies duly certified as correct of the following documents and records in the above-entitled cause in connection with the petition for review by the said Circuit Court of Appeals for the Eighth Circuit, heretofore filed by the Commissioner of Internal Revenue:

1. Docket entries of the proceedings before the Board.

2. Pleadings before the Board: (a) Petition, including annexed copy of deficiency letter; (b) Answer.

3. Findings of fact, opinion and decision of the Board.

4. Stipulation of facts.

5. Petition for review, together with proof of service of notice of filing petition for review and of service of a copy of petition for review:

6. Orders enlarging time for the preparation of the evidence and for the transmission and delivery of the record not included in record.

7. This praecipe.

(Signed) J. P. Wenchel, R. L. W. J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue.

Service of a copy of the within praecipe is hereby admitted this 18 day of August 1942.

(S.) Leland W. Scott, (S.) John W. Windhorst, Attorneys for Respondent on Review.

[fol. 52] UNITED STATES BOARD OF TAX APPEALS, WASHINGTON

Docket No. 106567

COMMISSIONER OF INTERNAL REVENUE, Petitioner,

v.

E. W. DOBSON, Respondent

CERTIFICATE

I, B. D. Gamble, clerk of the U. S. Board of Tax Appeals, do hereby certify that the foregoing pages, 1 to 69, inclusive, contain and are a true copy of the transcript of record, papers, and proceedings on file and of record in my office as called for by the Praecipe in the appeal (or appeals) as above numbered and entitled.

In testimony whereof, I hereunto set my hand and affix the seal of the United States Board of Tax Appeals, at-peals, at Washington, in the District of Columbia, this 1st day of September 1942.

B. D. Gamble, Clerk, United States Board of Tax Appeals. (Seal.)

UNITED STATES BOARD of TAX APPEALS

Docket No. 106553

JOHN V. DOBSON, Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent

Docket No. 106553

COMMISSIONER OF INTERNAL REVENUE, Petitioner,

v.

E. W. DOBSON, Respondent

ORDER ENLARGING TIME

For cause appearing of record, it is ordered that the time for transmission and delivery of the record *sur* petition for

review of the above entitled proceeding in the United States [fol. 53] Circuit Court of Appeals, Eighth Circuit, is extended to October 8, 1942.

(Signed) John W. Kern, Member.

Dated: Wash., D. C., Aug. 19, 1942.
1j.

Now, Aug. 31, 1942 the foregoing order is certified from the record as a true copy.

B. D. Gamble, Clerk, U. S. Board of Tax Appeals.

[Endorsed] Filed in U. S. Circuit Court of Appeals on September 2, 1942.

Before United States Board of Tax Appeals

Docket No. 106553

John V. Dobson, Petitioner,

v.

Commissioner of Internal Revenue, Respondent

For Taxpayer: Leland W. Scott, John W. Windhorst.
For Comm'r: S. U. Hiken, Esq.

Docket Entries

1941

Mar. 3—Petition received and filed. Taxpayer notified. Fee paid.
Mar. 3—Copy of petition served on General Counsel.
Mar. 3—Request for Circuit hearing in St. Paul, Minn. filed by taxpayer. 3/3/41 Copy served.
Mar. 31—Answer filed by G. C.
Apr. 3—Copy of answer served on taxpayer. (St. Paul, Minn.)
Apr. 28—Hearing set June 16, 1941, St. Paul, Minn.
June 18—Hearing had before Mr. Turner on the merits submitted. Stipulations as to the facts filed. Briefs due Aug. 2, 1941. Reply briefs August 18, 1941.
July 25—Brief filed by taxpayer.
July 28—Motion for extension to Aug. 15, 1941 to file brief filed by G. C. 7/31/41 Granted.

Aug. 2—Transcript of hearing 6/18/41 filed.
Aug. 11—Motion for additional extension to Aug. 30, 1941 to file brief filed by G. C.
[fol. 54]
Aug. 14—Motion for additional extension to Aug. 30, 1941 to file brief granted.
Aug. 29—Brief filed by G. C.
Sept. 2—Copy of brief served on G. C.
Sept. 13—Reply brief filed by taxpayer. 9/15/41 copy served.

1942

Mar. 27—Opinion rendered. Turner, Div. 8. Decision will be entered under Rule 50. 3/30/42 Copy served.
Apr. 17—Agreed computation filed.
Apr. 22—Decision entered. Murdock, Div. 3.
July 10—Petition for review by U. S. Cir. Ct. of Ap. 8th Circuit filed by G. C.
July 21—Proof of service filed by G. C.
July 20—Petition for review by U. S. Cir. Ct. of Ap. 8th Circuit with assignments of error filed by taxpayer.
July 22—Proof of service filed.
Aug. 13—Joint designation of record filed.
Aug. 19—Order enlarging time to Oct. 8, 1942 to transmit and deliver the record entered.

UNITED STATES BOARD OF TAX APPEALS

Docket No. 106553

JOHN V. DOBSON, Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent

Received Mar. 3, 1941. U. S. Board of Tax Appeals.

PETITION

The above named Petitioner hereby petitions for a redetermination of the deficiency set forth by the Commissioner of Internal Revenue in his Notice of Deficiency

dated December 26, 1940, and as a basis for the proceeding alleges:

I

The Petitioner, John V. Dobson, is an individual residing in the City of Minneapolis, County of Hennepin, and State of Minnesota. On or about March 15, 1940, Petitioner filed an income tax return for the calendar year 1939 with the Collector of Internal Revenue of the United States in and for the District of Minnesota.

[fol. 55]

II

The Notice of Deficiency, a copy of which, marked Exhibit A, is attached hereto and hereby made a part hereof, was mailed to Petitioner on December 26, 1940. The taxes in controversy are income taxes for the calendar year 1939 asserted against the Petitioner by said notice.

III

The Notice of Deficiency determined that Petitioner's income tax liability for the calendar year 1939 was $11,509.49. Of this amount $2,401.43 was paid by the Petitioner during the calendar year 1940 and Respondent determined a deficiency in Petitioner's income tax liability for the calendar year 1939 in the sum of $9,108.06. The entire amount of said deficiency is in controversy.

IV

The determination of tax set forth in said Notice of Deficiency is based on the following errors:

(a) Respondent erred in determining that the entire amount of $33,404, recovered by Petitioner during the calendar year 1939 from National City Company, constituted income taxable to the Petitioner.

(b) Respondent erred in determining that $33,246.96 of said $33,404 recovered by Petitioner from National City Company did not constitute a return of capital to the Petitioner.

(c) Respondent erred in determining that Petitioner realized income in excess of the sum of $157.04 as the result of the recovery by Petitioner of said $33,404 from said National City Company.

(d) Respondent erred in determining that the income realized by Petitioner as the result of said recovery from National City Company did not constitute capital gain under the provisions of Section 117 of the Internal Revenue Code.

(e) Respondent erred in determining that there is a deficiency in Petitioner's income tax liability for the calendar year 1939.

V

The facts upon which Petitioner relies as a basis for this proceeding are as follows:

(a) On or about the dates and for the amounts set forth below the Petitioner purchased and sold stock of National City Bank of New York:

[fol. 56] 1. On January 17, 1929, Petitioner purchased 50 shares at a cost of $14,050.

2. On April 22, 1929, Petitioner purchased 50 shares at a cost of $18,850.

3. On October 8, 1929, Petitioner purchased 100 shares at a cost of $49,500.

4. On October 29, 1929, Petitioner sold the 200 shares of stock purchased at items 1, 2 and 3 above for $7,400.

5. On October 29, 1929, Petitioner purchased 40 shares at a cost of $14,000.

6. On October 30, 1929, Petitioner sold the 40 shares purchased at item 5 above for $17,999.48.

7. On November 8, 1929, Petitioner purchased 200 shares at a cost of $66,000.

8. On December 3, 1930, Petitioner sold the 200 shares purchased at item 7 above for $20,897.44.

9. On July 3, 1931, Petitioner purchased 200 shares at a cost of $17,700.

10. On July 13, 1931, Petitioner sold 200 shares purchased at item 9 above for $16,000.

The cost of the purchases described above represents the actual cash outlay of the Petitioner and does not necessarily

determine the income tax cost of said stock to the Petitioner inasmuch as some of the above sales represent wash sales of said stock, thereby increasing the cost of subsequent purchases of said stock as required by the Revenue Act of 1928.

(b) On or about March 15, 1931, the Petitioner filed with the collector of Internal Revenue of the United States in and for the District of Minnesota an income tax return for the calendar year 1930. Said income tax return disclosed the following gross income and deductions therefrom:

Income:		
Salaries	$14,500.00	
Dividends on stock of domestic corporations	23,659.45	
Total income		$38,159.45
Deductions:		
Interest paid	$3,273.23	
Taxes paid	875.69	
Bad debts	1,783.00	
Loss on sale of stock of National City Bank of New York	62,012.56	
Total Deductions		67,944.48
Net income		None

Except as hereinafter set forth with respect to the loss arising upon the sale of stock of National City Bank of New York the income and deductions set forth above are a [fol. 57] true and correct statement of Petitioner's net income for the calendar year 1930 and the Respondent has not made any changes therein. The loss sustained on the sale of stock of National City Bank of New York in the sum of $62,012.56, described in said return, was realized from the sale of 200 shares of said stock for the sum of $20,897.44 on December 3, 1930, as set forth at Item V (a) 8 above. In Petitioner's income tax return for said calendar year 1930 the cost of said stock was set forth as $82,910. The correct income tax cost of said stock was $78,857.38 and the Peti-

tioner therefore sustained a loss upon the sale of said stock in 1930 in the sum of $57,673.94.

(c) On or about March 15, 1932, Petitioner filed an income tax return for the calendar year 1931 with the Collector of Internal Revenue of the United States in and for the District of Minnesota. In said return Petitioner disclosed a net income of $17,514.27 and a tax thereon of $125.43 which was paid to said Collector of Internal Revenue during the calendar year 1932. On or about July 13, 1931, Petitioner sold 200 shares of the stock of National City Bank of New York as set forth at Item V (a) 10 above. Petitioner thereby realized a loss of $1,700, none of which was deducted by Petitioner in computing said net income disclosed in said income tax return for the calendar year 1931. Except for the failure to deduct said loss on the sale of said stock, the income deductions and credits set forth in Petitioner's income tax return for the calendar year 1931 are true and correct and the Respondent has not made any changes therein.

(d) During the calendar year 1939 the Petitioner instituted suit against the National City Company for the recovery of the purchase price of stock of National City Bank of New York purchased from said National City Company on April 22, 1929, October 8, 1929, November 8, 1929, and July 3, 1931, as set forth in paragraph V (a) 2, 3, 7, and 9 above. Said suit was dismissed and Petitioner received as consideration for said dismissal the net amount of $33,404. $157.04 of said amount was recovered with respect to 40 shares of the stock purchased on April 22, 1929 (Item V (a) 2 above); $32,294.96 was recovered with respect to 10 shares of the stock purchased on April 22, 1929 (Item V (a) 2 above), the 100 shares of stock purchased on October 8, 1929 (Item V (a) 3 above), and the 200 shares of stock purchased on November 8, 1929 (Item V (a) 7 above); and $952.00 was recovered with respect to the 200 shares of stock purchased on July 3, 1931 (Item V (a) 9 above).

(e) Except for said recovery of $33,404 during the calendar year 1939 Petitioner has not been reimbursed in any [fol. 58] manner for the loss sustained on the sale of stock of National City Bank of New York as set forth in paragraph V (a) above.

Wherefore, Petitioner prays that this Board may hear the proceedings and decide that:

(a) Respondent erred in determining that the entire amount of $33,404, recovered by Petitioner during the calendar year 1939 from National City Company, constituted income taxable to the Petitioner.

(b) Respondent erred in determining that $33,246.96 of said $33,404 recovered by Petitioner from National City Company did not constitute a return of capital to the Petitioner.

(c) Respondent erred in determining that Petitioner realized income in excess of the sum of $157.04 as the result of the recovery by Petitioner of said $33,404 from said National City Company.

(d) Respondent erred in determining that the income realized by Petitioner as the result of said recovery from National City Company did not constitute capital gain under the provisions of Section 117 of the Internal Revenue Code.

(e) Respondent erred in determining that there is a deficiency in Petitioner's income tax liability for the calendar year 1939.

Leland W. Scott, John W. Windhorst, 1300 First National-Soo Line Bldg., Minneapolis, Minnesota, Attorneys for Petitioner.

STATE OF MINNESOTA,
County of Hennepin, ss:

John V. Dobson, being duly sworn, on oath deposes and says that he is the Petitioner in the above entitled action; that he has read the foregoing Petition and knows the contents thereof; that the same is true of his own knowledge, except as to those matters therein stated on information and belief and as to such matters he believes it to be true.

John V. Dobson.

Subscribed and sworn to before me this 27 day of February 1941. W. J. Murphy, Notary Public, Hennepin County, Minn. My Commission expires December 28, 1941. (Notarial seal.)

[fol. 59] EXHIBIT "A" TO PETITION

Office of Internal Revenue Agent in Charge, St. Paul Division, 800 Post Office Bldg.

Treasury Department,
Internal Revenue Service,
St. Paul, Minnesota, Dec. 26, 1940.

Collection District: Minnesota

Mr. John V. Dobson, *2639 Lake of Isles Blvd., Minneapolis, Minnesota.*

SIR:

You are advised that the determination of your income tax liability for the taxable year (x) 1939 discloses a deficiency of $9,108.06 as shown in the statement attached.

In accordance with the provisions of existing internal revenue laws, notice is hereby given of the deficiency mentioned.

Within 90 days (not counting Sunday or a legal holiday in the District of Columbia as the 90th day) from the date of the mailing of this letter, you may file a petition with the United States Board of Tax Appeals for a redetermination of the deficiency.

Should you not desire to file a petition, you are requested to execute the enclosed form and forward it to the internal revenue agent in charge, St. Paul, Minnesota, for the attention of LGE–90D. The signing and filing of this form will expedite the closing of your return(s) by permitting an early assessment of the deficiency, and will prevent the accumulation of interest, since the interest period terminates 30 days after filing the form, or on the date assessment is made, whichever is earlier.

Respectfully, Guy T. Helvering, Commissioner, by C. W. Rink, Internal Revenue Agent in Charge.

Enclosures: Statement. Form of Waiver.

LGE/mrr.
GPO. 2–17679.

[fol. 60] STATEMENT

Mr. John V. Dobson, 2639 Lake of Isles Boulevard,
Minneapolis, Minnesota

Tax Liability for Taxable Year Ended December 31, 1939

Income tax: Liability $11,509.49; assessed $2,401.43; deficiency $9,108.06.

In making this determination of your income tax liability, careful consideration has been given to the report of examination dated November 5, 1940.

Adjustments to Net Income

Net income as disclosed by return	$24,583.01
Unallowable deductions and additional income:	
(a) Recovery	33,246.96
Net income adjusted	57,829.97

Explanation of Adjustments

(a) In 1929 you purchased 200 shares of National City Bank stock and sold same at a loss in 1930. During 1939 you received a net amount of $33,404.00 in settlement of a suit brought against the National City Company based on contention that the original sale of this stock to you was illegal, being in violation of the securities laws of the State of Minnesota governing such sales.

It is held that his settlement constitutes taxable income in its entirety.

Net amount received	$33,404.00
Reported	157.04
Adjustment	33,246.96

Computation of Tax

Adjusted net income	$57,829.97
Less: Personal exemption	2,500.00
Balance (surtax net income)	55,329.97
Less: Earned income credit—maximum	1,400.00
Balance subject to normal tax	53,929.97
Normal tax at 4%	2,157.20
Surtax on $55,329.97	9,352.29
Total Tax	11,509.49
Total tax assessable	11,509.49
Tax previously assessed—Acct. No. 202181	2,401.43
Deficiency in income tax	9,108.06

[fol. 61] UNITED STATES BOARD OF TAX APPEALS

Docket No. 106553

JOHN V. DOBSON, Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent

Received Mar. 31, 1941. U. S. Board of Tax Appeals

ANSWER

Now comes the Commissioner of Internal Revenue, by his attorney, J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue, and for answer to the petition filed herein admits, denies and alleges as follows:

I and II. Admits the allegations contained in paragraphs I and II of the petition.

III. Admits that in the notice of deficiency it was determined that petitioner's income tax liability for the calendar

year 1939 is $11,509.49; admits that respondent determined a deficiency in petitioner's income tax liability for the calendar year 1939 in the sum of $9,108.06; admits that the entire amount of said deficiency is in controversy; denies the remaining allegations contained in paragraph III of the petition.

IV. (a) to (e), inclusive. Denies that the respondent erred as alleged in subparagraphs (a) to (e), inclusive, of paragraph IV of the petition.

V. (a) Admits that sometime in 1929 the petitioner purchased 200 shares of stock of National City Bank; admits that the petitioner sold said stock at a loss in 1930; denies the remaining allegations contained in subparagraph (a) of paragraph V of the petition.

V. (b) Denies the allegations contained in subparagraph (b) of paragraph V of the petition, except it is admitted that in 1930 the petitioner sustained a substantial loss, the exact amount of which is unknown to the respondent, on the sale sometime in that year of 200 shares of National City Bank stock purchased by the petitioner sometime in 1929.

V. (c) Denies the allegations contained in subparagraph (c) of paragraph V of the petition.

V. (d) Admits that during the calendar year 1939 the petitioner instituted a suit against the National City Company; admits that petitioner received the net amount of $33,404.00 in 1939 on account of the institution of said suit; [fol. 62] denies the remaining allegations contained in subparagraph (d) of paragraph V of the petition.

V. (e) Denies the allegations contained in subparagraph (e) of paragraph V of the petition.

Denies generally and specifically each and every allegation contained in the petition not hereinbefore specifically admitted, qualified or denied.

Wherefore, respondent prays that the Board redetermine the deficiency herein to be the amount determined by the Commissioner, viz.: $9,108.06 in respect of income taxes for the taxable year 1939.

(Signed) J. P. Wenchel, S. U. H., J. P. Wenchel,
Chief Counsel, Bureau of Internal Revenue.

Of Counsel: F. R. Shearer, Division Counsel; S. U. Hiken, Special Attorney, Bureau of Internal Revenue.

UNITED STATES BOARD OF TAX APPEALS

JOHN V. DOBSON, Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent

Docket No. 106553. Promulgated March 27, 1942

By reason of a loss in 1930 on the sale of certain bank stock, deduction for which was claimed and allowed, petitioner sustained and reported a net loss for that year. Charging fraud, he brought suit in 1938 for rescission of the contract whereby the said bank stock had been purchased. In 1939 he received in settlement of the said suit, an amount less than the loss sustained on the sale of stock but greater than his 1930 net loss. *Held*, that the amount recovered in 1939 constitutes taxable income in the year of recovery to the extent that the amount recovered is in excess of the 1930 net loss, and that such income is taxable as ordinary income.

John W. Windhorst, Esq., and Leland W. Scott, Esq., for the petitioner.

S. U. Hiken, Esq., for the respondent.

[fol. 63] OPINION

Turner: The respondent determined a deficiency in income tax for the year 1939 in the amount of $9,108.06. The question presented is whether a sum of money, or any part thereof, recovered by the petitioner in the taxable year as a result of litigation involving certain stock transactions in prior years constitutes a return of capital, as contended by petitioner, or taxable income, as contended by respondent. The parties have filed a written stipulation of facts, with certain exhibits attached thereto, and the Board adopts such stipulation as its findings of fact. We shall recite only the facts deemed necessary to discussion of the issue presented.

Petitioner, a resident of Minneapolis, Minnesota, filed his 1939 income tax return with the collector of internal revenue for the district of Minnesota.

At various times in 1929 petitioner purchased, in transactions entered into for profit, a total of 440 shares of the capital stock of the National City Bank of New York. The stock also carried certain beneficial interests in the stock of

the National City Co. of New York. The purchases were made in the State of Minnesota from the National City Co.

During the year 1929 petitioner sold a total of 240 shares of the stock, 90 shares of which resulted in a taxable gain of $8,168.44 and was so treated in closing petitioner's income tax liability for 1929. The sale of the remaining 150 shares in 1929 resulted in a loss of $13,168.44, properly disallowed as a deduction in closing petitioner's 1929 income tax liability because of the wash sales provisions of the Revenue Act of 1928.

In 1930 petitioner sold the remaining 200 shares of the stock for $20,897.44. These shares had actually cost the petitioner $70,000, but, because of the wash sales in 1929 which resulted in nondeductible losses for that year, the petitioner's basis for determining the amount of loss sustained in 1930 was $70,000 plus $13,168.44, or $83,168.44. The 1930 sale resulted in a deductible loss by the petitioner in the amount of $62,271, which was allowed by the respondent as a deduction in closing petitioner's income tax liability for that year.

On July 3, 1931, petitioner purchased 200 shares of the bank stock at a cost of $17,700, and on July 13, 1931, sold the said shares for $16,000, thereby sustaining a loss of $1,700 which was deductible for 1931, but was not claimed as a deduction. Upon audit of the return, no deduction was allowed by the respondent by reason of the loss realized on the sale, but had such loss been claimed as a deduction it would have been allowed by the respondent and would have re- [fol. 64] duced the income tax liability of petitioner for the year 1931, but would not have eliminated entirely liability to tax. Petitioner's 1931 return disclosed net income of $17,514.27, and a tax thereon of $125.43, which was paid to the collector during the year 1932.

Until September 1937 the petitioner regarded the aforesaid purchases and sales as closed and completed transactions. During that month petitioner learned for the first time that the stock had not been registered under the Minnesota Blue Sky Laws, and further learned for the first time facts which led him to believe that the sales by the company to him might have been fraudulent. On or about July 9, 1938, the petitioner filed a suit against the National City Co. in an effort to recover the amounts which he had paid for the stock in 1929 and 1931, alleging that the stock had been sold to him without having been registered in accordance

with the requirements of the Minnesota Blue Sky Laws and that the sales had been fraudulent. He asked for a decission of the entire transaction and tendered to the defendant company the proceeds of the stock or an equivalent number of shares of stock of the bank, plus interest and dividends received.

In 1939 the suit was settled by a net payment of $33,404 by the company to the petitioner, and upon receipt thereof the suit was dismissed, with prejudice, pursuant to a stipulation between the parties. Of the total net recovery, $157.04 related to 40 shares of stock which are not here involved and is conceded to be taxable income. Of the remainder, $32,294.96 is allocable to the stock sold by the petitioner in 1930 and the balance of $952 is allocable to the stock sold by petitioner in 1931.

If the entire deduction of $62,271, allowed as a deduction in connection with petitioner's 1930 Federal income tax liability had been disallowed, there would have been net income in the amount of $32,227.53 and a deficiency in petitioner's income tax for 1930 would have resulted in the amount of $1,232.75, computed as follows:

Net loss		($30,043.47)
Add: Loss on National City Bank stock, eliminated		62,271.00
Net income revised		32,227.53
Less:		
Dividends	$23,659.45	
Personal exemption	3,500.00	
Credit for dependents	1,200.00	28,359.45
		3,868.08
Normal tax: 1½% of $3,868.04		$57.02
Surtax on $32,227.53		1,240.48
Total		1,297.50
[fol. 65] Less: Earned income credit		$64.75
Total tax assessable		1,232.75
Assessed		0.00
Deficiency		1,232.75

If in addition to the $20,897.44 actually received on the sale of the stock in 1930 petitioner had received $32,294.96, being the amount recovered in 1939 in respect of the stock sold in 1930, his deductible loss for 1930 from the sale of the said stock would have been $29,976.04 and he would have had net income in the amount of $2,251.49. Due to certain credits allowable, however, his income tax for 1930 would have been zero, shown as follows:

Net loss		($30,043.47)
Add: Entire amount recovered in 1939 in reduction of loss on stock sold in 1930		32,294.96
Net income revised		2,251.49
Less:		
Personal exemption	$3,500.00	
Credit for dependents	1,200.00	
Total		4,700.00
Balance subject to tax		none
Total tax assessable		none
Tax assessed		none
Deficiency		none

Throughout the year 1939 adjustment of petitioner's income tax liability for 1930 was barred by the statute of limitations.

In his income tax return for 1939 the petitioner reported income of only $157.04 on account of the recovery of $33,404. In the deficiency notice the respondent adjusted the amount of gross income reported by adding $33,246.96 and thereby treating the entire amount of petitioner's net recovery of $33,404 as ordinary income.

Since addition to 1930 income of an amount equal to that recovered in 1939 in respect of the stock sold in 1930 would not have resulted in any amount of income tax for 1930, it is the claim of the petitioner that no part of the said recovery constituted taxable income for 1939, even though the loss deduction of $62,271 claimed and allowed for 1930 in respect of the said sale did serve to offset taxable income in the amount of $32,227.53, and even though there would have

been net income in 1930 in the amount of $2,251.49 instead of a net loss if upon the sale of stock in that year petitioner had received an additional amount equal to that recovered in 1939. In the alternative, petitioner contends that if the amount recovered is taxable it is taxable as capital gain. The respondent contends that the amount recovered by the petitioner which is allocable to the 1930 sale is taxable as [fol. 66] ordinary gain and that it is wholly immaterial whether petitioner realized any tax benefit from the deduction taken in the prior year but that in any event the petitioner did realize a tax benefit to the extent that the deduction taken in the prior year operated to offset taxable income.

In Estate of James N. Collins, 46 B. T. A.—(Mar. 27, 1942), concurrently decided, we have considered the nature and character of transactions and recoveries such as are here involved and have reviewed the controlling decisions. Where there is recovery in respect of a loss sustained in an earlier year and a deduction of such loss claimed and allowed for the earlier year had effected an offset in taxable income, the amount recovered in the later year should be included in taxable income for the year of recovery, the reason being that even though the subsequent recovery is in the nature of a capital recovery the prior deduction of the amount of the loss from taxable income has for income tax purposes already given the taxpayer a recoupment of said loss out of taxable income and the subsequent recovery, being in the nature of a replacement of taxable income, is equivalent to gain to the taxpayer. National Bank of Commerce of Seattle v. Commissioner, 115 Fed. (2d) 875, affirming 40 B. T. A. 72. But where the deduction claimed and allowed in the prior year did not effect an offset of taxable income, the amount recovered in a later year does not constitute taxable income for the year of recovery. Estate of James N. Collins, supra. In the instant case the deduction for 1930 of the loss sustained upon the sale of the National City Bank stock resulted in a net loss to the petitioner for that year of $30,043.57, and to that extent the loss deduction claimed in 1930 did not effect an offset of taxable income. In 1939 the petitioner recovered in respect of such stock and in addition to the amount received upon its sale in 1930 the amount of $32,294.96. It is accordingly apparent that the deduction in 1930 of the amount recovered in 1939

did effect an offset in taxable income in the amount of $2,251.49, that amount being the excess of the 1939 recovery over the 1930 net less and to that extent the amount recovered in 1939 constitutes taxable income to the petitioner in the year of recovery. Central Loan & Investment Co., 39 B. T. A. 981; Amsco-Wire Products Corporation, 44 B. T. A. 717. Petitioner's contention that the income so realized should be taxed as capital gain is denied on authority of Avery R. Schiller, 43 B. T. A. 594.

With respect to the $952 recovered in 1939 in respect of the stock sold in 1931, the respondent on brief states: "For the purposes of the present case the respondent does not [fol. 67] press the issue that the amount of $952.00 of the recovery allocable to the stock which was sold in 1931 and on which no loss was claimed, constitutes taxable income, inasmuch as the principle enunciated in G. C. M. 22163, 1940-2 Cum. Bull. 76 is to the contrary."

Decision will be entered under Rule 50.

UNITED STATES BOARD OF TAX APPEALS, WASHINGTON

Docket No. 106553

JOHN V. DOBSON, Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent

DECISION

Pursuant to the Findings of Fact and Opinion of the Board promulgated March 27, 1942, the parties herein having on April 17, 1942, filed an agreed recomputation of tax in accordance therewith, it is

Ordered and decided: That there is a deficiency in income tax for the year 1939 in the amount of $472.82.

(S.) J. E. Murdock, Member.

Entered April 22, 1942.

UNITED STATES CIRCUIT COURT OF APPEALS FOR THE EIGHTH CIRCUIT

B. T. A. Docket No. 106553

GUY T. HELVERING, Commissioner of Internal Revenue,
Petitioner on Review,

vs.

JOHN V. DOBSON, Respondent on Review

Received July 10, 1942, U. S. Board of Tax Appeals.

PETITION FOR REVIEW

To the Honorable Judges of the United States Circuit Court of Appeals for the Eighth Circuit:

Guy T. Helvering, Commissioner of Internal Revenue, holding office by virtue of the laws of the United States, hereby petitions for review by the United States Circuit Court of Appeals for the Eighth Circuit of the decision [fol. 68] entered by the United States Board of Tax Appeals on April 22, 1942, ordering and deciding that there is a deficiency of $472.82 in income tax for the year 1939 due from the taxpayer, John V. Dobson, the respondent on review. The taxpayer's income tax return for the year 1939 was filed with the Collector of Internal Revenue for the District of Minnesota, located at St. Paul, Minnesota.

The question presented is whether the taxpayer received taxable income in the amount of $30,043.57 which is an allocable portion of the sum of $33,404 received by him in 1939 in compromise of a suit filed against the National City Company of New York for rescission of contracts entered into in 1929 and 1931 for the purchase of bank stock. The taxpayer sold part of the stock in 1930 at a loss which he claimed as a deduction in his income tax return for that year. Until September 1937 the taxpayer regarded the purchases and sales of the stock as closed and completed transactions, but upon learning that the stock had not been registered under the Massachusetts Blue Sky Laws, instituted the suit which led to the recovery in 1939 of the sum of $33,404, of which he concedes $157.04 constitutes taxable income, and of which the Commissioner concedes that $952 does not constitute taxable income. The balance of the re-

covery amounting to $32,294.96 was not reported as taxable income by the taxpayer and was included in taxable income in the notice of deficiency issued by the Commissioner.

The United States Board of Tax Appeals reversed the Commissioner's determination and held that only $2,251.49 of the balance of the recovery in the amount of $32,294.96 is includable in taxable income for 1939. The Board refused to sanction the inclusion of any part of the remainder of the recovery amounting to $30,043.57 in taxable income for the year 1939, for the reason that the taxpayer did not derive a tax benefit from the deduction of the loss taken in 1930.

The Commissioner avers that in the record and proceedings before the United States Board of Tax Appeals and in the opinion and decision rendered and entered by the United States Board of Tax Appeals manifest error occurred and intervened to the prejudice of the Commissioner who now assigns the following points on which he intends to rely in this proceeding:

The United States Board of Tax Appeals erred—

(1) In holding and deciding that no part of $30,043.47 recovered by the taxpayer in 1939 in settlement of a suit for rescission of contracts for the purchase of stock in 1929 and 1931, part of which stock was sold in 1930 and losses therefrom were claimed and allowed as deductions from gross [fol. 69] income in determining the income tax liability of the taxpayer for the year 1930, should be included in the taxpayer's gross income for 1939.

(2) In failing to hold and decide that $30,043.47 of the amount recovered by the taxpayer in 1939 in settlement of a suit for rescission of contracts for the purchase of stock in 1929 and 1931, part of which stock was sold in 1930 and losses therefrom were claimed and allowed as deductions from gross income in determining the income tax liability of the taxpayer for the year 1930, constituted taxable income for 1939.

(3) In entering its decision wherein it ordered and decided that there is a deficiency in income tax due from this taxpayer in the amount of $472.82 for the calendar year 1939.

(4) In failing and refusing to enter its decision redetermining that there is a deficiency in income tax due by the taxpayer in the amount of $9,108.06.

(5) In that its decision is not supported by the evidence.

(6) In that its decision is contrary to law and regulations.

(Sgd.) Samuel O. Clark, Jr., Assistant Attorney General; (Signed) J. P. Wenchel, R. L. W., Chief Counsel, Bureau of Internal Revenue, Attorneys for Petitioner on Review.

ERT/mar 6/10/42.

UNITED STATES CIRCUIT COURT OF APPEALS FOR THE EIGHTH CIRCUIT

B. T. A. Docket No. 106553

GUY T. HELVERING, Commissioner of Internal Revenue, Petitioner on Review,

vs.

JOHN V. DOBSON, Respondent on Review

Received, July 21, 1942, U. S. Board of Tax Appeals.

NOTICE OF FILING PETITION FOR REVIEW

To John V. Dobson, 2639 Lake of Isles Blvd., Minneapolis, Minn.:

You are hereby notified that the Commissioner of Internal Revenue did, on the 10th day of July, 1942, file with the [fol. 70] United States Board of Tax Appeals, at Washington, D. C., a petition for review by the United States Circuit Court of Appeals for the Eighth Circuit of the decision of the Board heretofore rendered in the above-entitled cause. A copy of the petition for review as filed is hereto attached and served upon you.

Dated this 10th day of July 1942.

(Signed) J. P. Wenchel, R. L. W., Chief Counsel, Bureau of Internal Revenue.

Personal service of the above and foregoing notice, together with a copy of the petition for review mentioned therein is hereby acknowledged this 14th day of July 1942.

(S.) John V. Dobson, Respondent on Review.

RHT/mar 6/24/42.

UNITED STATES CIRCUIT COURT OF APPEALS, EIGHTH CIRCUIT

B. T. A. Docket No. 106553

JOHN V. DOBSON, Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE, Respondent

PETITION FOR REVIEW AND ASSIGNMENTS OF ERROR

To the Honorable Judges of the United States Circuit Court of Appeals for the Eighth Circuit:

Now comes John V. Dobson, by his attorneys, Leland W. Scott and John W. Windhorst, and respectfully shows:

I

JURISDICTION

The petitioner on review is an individual residing in the City of Minneapolis, County of Hennepin, State of Minnesota. The respondent on review holds his office under and by virtue of the laws of the United States. An income tax return was filed by the Petitioner for the calendar year 1939 on or about March 15, 1940, with the Collector of Internal Revenue for the District of Minnesota in St. Paul, Minnesota, whose office is located within the judicial district of the United States Circuit Court of Appeals for the Eighth Circuit.

[fol. 71]

II

NATURE OF CONTROVERSY

On December 26, 1940, the Commissioner forwarded to the Petitioner by registered mail a notice of deficiency wherein the Petitioner was notified of a deficiency in the amount of $9,108.06 in his income tax liability for the year 1939.

Thereafter, on March 3, 1941, the Petitioner filed with the Board of Tax Appeals a petition for redetermination of the proposed deficiency for the year 1939. On March 31, 1941, the Commissioner filed with the Board of Tax Appeals his answer to the petition of the Petitioner. The proceeding came on to be heard before a division of the Board of Tax Appeals sitting in St. Paul, Minnesota, on June 18, 1941.

The questions presented are (1) whether the Petitioner must include in his taxable gross income for the calendar year 1939 the amount of $2,251.49 representing a portion of the amount received in settlement of a suit for rescission of a purchase of National City Bank of New York stock by the Petitioner from National City Company, and (2) if said amount is to be included in Petitioner's taxable income for 1939, whether it is to be treated as ordinary income or as capital gain under Section 117 of the Internal Revenue Code.

On March 27, 1942, the Board of Tax Appeals promulgated its opinion wherein it was held that the Petitioner was taxable on the amount of $2,251.49 of the total received in settlement of damage suits in 1939 and excluded by the Petitioner from the taxable income reported in his return for 1939. The Board further held that said $2,251.49 was taxable as ordinary income rather than capital gain. On April 22, 1942, the board entered its decision and order that there was a deficiency of $472.82 in the Petitioner's income tax liability for the calendar year 1939. On or about April 28, 1942, the Petitioner paid the entire amount of said deficiency, plus interest in the amount of $60.27, to the Collector of Internal Revenue for the District of Minnesota.

The facts shortly stated are as follows: At various times in 1929 the petitioner purchased from National City Company a total of 440 shares of capital stock in the National City Bank of New York. During 1930 the Petitioner sold a portion of this stock for $20,897.44. This stock had cost the Petitioner $83,168.44 and Petitioner thereby sustained a loss on said stock in the sum of $62,271, which amount was allowed by the Commissioner as a deduction in determining the Petitioner's income tax liability for 1930. In [fol. 72] 1938 Petitioner commenced a suit against the National City Company wherein he sought to rescind the purchase of the stock for alleged fraud on the part of the de-

fendant and violations of the Minnesota Blue Sky Law. The action was settled during the year 1939 by a net payment of $33,404 by the National City Company to the Petitioner. Of the amount received in settlement, $32,294.96 is allocable to the stock sold by the Petitioner in 1930. This latter amount was not included in the taxable income reported by Petitioner in his 1939 income tax return. If the deductible loss suffered during 1930 upon the sale of National City Bank stock were reduced by the amount of 1939 recovery allocable to the shares sold during 1930, the 1930 income tax return of the Petitioner would have shown a net income of $2,251.49. Because of a personal exemption in the amount of $3,500 and a credit for dependents in the amount of $1,200, the tax liability of the Petitioner for 1930 under these circumstances would have been zero. The loss on the stock sales in 1930, to the extent compensated for by the 1939 settlement, resulted in no tax saving to the Petitioner.

III

Points upon Which Petitioner Intends to Rely

Petitioner is aggrieved at the decision of the Board of Tax Appeals and says that in the proceeding before the Board and in the opinion and decision aforesaid manifest error occurred and intervened to his prejudice and he assigns as error the following:

1. The Board of Tax Appeals erred in determining that there is a deficiency of $472.82 in Petitioner's income tax liability for 1939, in that its decision is contrary to law.

2. The Board of Tax Appeals erred in finding that a part of the amount received in settlement of the legal action against the National City Company in 1939, to the extent of $2,251.49, was includable in the Petitioner's taxable income for the calendar year 1939 under Section 22 of the Internal Revenue Code.

3. The Board of Tax Appeals erred in finding that a part of the amount received in settlement of the legal action against the National City Company in 1939 in the amount of $2,251.49 was to be treated as ordinary income rather than capital gain under Section 117 of the Internal Revenue Code.

4. The Board of Tax Appeals erred in failing to find that none of the amount recovered in settlement of the legal ac-

tion against the National City Company in 1939 and allocable to the purchase price of stock of National City Bank [fol. 73] of New York which was sold in 1930 was includable in the taxable income of the Petitioner in 1939, under Sec. 22 of the Internal Revenue Code.

5. The Board of Tax Appeals erred in entering judgment that there was a deficiency of $472.82 in the amount of Petitioner's income tax liability for the calendar year 1939, instead of entering judgment of no deficiency for said year, in that the uncontradicted evidence warrants no other conclusion.

Wherefore, The Petitioner requests that the aforesaid decision of the Board of Tax Appeals be reviewed by the United States Circuit Court of Appeals for the Eighth Circuit; that a transcript of record be prepared in accordance with law and the rules of this Court and transmitted to the Clerk of said Court for filing; and that appropriate action be taken to the end that errors complained of may be reviewed and corrected by the Court.

Leland W. Scott, John W. Windhorst, Counsel for Petitioner, 1300 First National-Soo Line Building, Minneapolis, Minnesota.

* * * * * * *

Duly sworn to by John W. Windhorst. Jurat omitted in printing.

[fol. 74] IN THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE EIGHTH CIRCUIT

B. T. A. Docket No. 106553

JOHN V. DOBSON, Petitioner on Review,

vs.

COMMISSIONER OF INTERNAL REVENUE, Respondent on Review

Received July 22, 1942. U. S. Board of Tax Appeals.

NOTICE OF FILING PETITION FOR REVEIW AND STATEMENT OF POINTS

To J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue:

You are hereby notified that John V. Dobson did, on the 20th day of July 1942, file with the Clerk of the United

States Board of Tax Appeals, at Washington, D. C., a petition for review by the United States Circuit Court of Appeals for the — Circuit, of the decision of the Board heretofore rendered in the above entitled case. Copies of the petition for review and the statement of points as filed are hereto attached and served upon you.

Dated this 21st day of July 1942.

(S.) B. D. Gamble, Clerk, U. S. Board of Tax Appeals.

Service of copy of Petition for Review and Statement of Points acknowledged this July 22, 1942.

J. P. Wenchel, Attorney for Respondent.

UNITED STATES BOARD OF TAX APPEALS

Docket No. 106553

JOHN V. DOBSON, Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE, Respondent

U. S. Board of Tax Appeals. Filed at hearing June 18, 1941.

STIPULATION OF FACTS

It is hereby stipulated and agreed by and between the parties hereto, by their respective counsel, that the follow- [fol. 75] ing facts shall be taken as true, provided, however, (1) that each of the parties hereto reserves the right to object to the admissibility in evidence of any of such facts on the ground of irrelevancy and immateriality and (2) that this stipulation shall be without prejudice to the right of either party to introduce other and further evidence not inconsistent herewith:

I

Petitioner, a resident of Minneapolis, Minnesota, filed, within the time required by law, his 1939 Federal income tax return with the Collector of Internal Revenue at St. Paul, Minnesota.

II

In 1929 the petitioner purchased at various times, in transactions entered into for profit, a total of 440 shares of the capital stock of National City Bank (hereinafter referred to as the stock), the purchases carrying with them, at no additional cost, proportionate beneficial interests in the stock of National City Company (of New York). In 1933 the name of the latter company was changed to City Company of New York, Inc. These purchases were made by the petitioner in the State of Minnesota from the National City Company.

III

During the year 1929 the petitioner sold a total of 240 shares of said stock. The sale of 90 of such shares resulted in a taxable gain of $8,168.44, so treated in closing petitioner's Federal income tax liability for 1929. The sales of the remaining 150 shares in 1929 resulted in a loss of $13,168,44, properly disallowed as a deduction in closing petitioner's 1929 Federal income tax liability because of the wash-sales provisions of the Revenue Act of 1928.

IV

In 1930 the petitioner sold the remaining 200 shares of said stock for $20,897.44. These shares had actually cost the petitioner $70,000.00, but because of the wash-sales in 1929 which resulted in nondeductible losses for that year the petitioner's basis for determining the amount of the loss which he sustained in 1930, for Federal income tax purposes, was $70,000.00 plus $13,168.44, or $83,168.44. This situation resulted in the realization by the petitioner of a deductible loss in the amount of $62,271.00 for 1930 which [fol. 76] was allowed by the respondent as a deduction in closing petitioner's income tax liability for said year.

V

On July 3, 1931, the petitioner purchased 200 shares of said stock at a cost of $17,700. On July 13, 1931, petitioner sold said 200 shares for $16,000 and thereby sustained a loss of $1,700 which was deductible by petitioner in his income tax return for the calendar year 1931, but which was not claimed by petitioner in his income tax for the calendar year 1931. Upon audit of said return, no amount was al-

lowed by respondent as a deduction by reason of the loss realized on said sales.

VI

Until September 1937, the Petitioner regarded the aforesaid purchases and sales as closed and completed transactions. In September 1937, the Petitioner learned for the first time that said stock had not been registered under the Minnesota Blue Sky laws and the Petitioner also learned for the first time of facts which led him to believe that said sales might have been fraudulent. Thereafter, and on or about July 9, 1938, the petitioner filed a suit against the National City Company in an effort to recover the amounts which he paid for the stock in 1929 and 1931. The petitioner's contentions in that suit were: (1) that the stock had been sold to him without having been registered in accordance with the requirements of the Minnesota Blue Sky laws, and (2) that the sales had been fraudulent. A copy of the complaint in said action is attached hereto, marked Exhibit A and made a part hereof the same as if fully set forth herein.

VII

This suit was settled by the payment to the petitioner in 1939 of $33,404 net, after the payment by him of attorneys' fees and other similar expenses. On March 28, 1939, pursuant to said settlement, a stipulation of dismissal with prejudice was executed by the parties to said action. A copy of said stipulation for dismissal, marked Exhibit B, is attached hereto and made a part hereof the same as if fully set forth herein.

Of said amount of $33,404, the sum of $157.04 was recovered with respect to forty shares of stock which is not here [fol. 77] involved and which is conceded to be taxable income: $32,294.96 of said amount is allocable to stock sold by the petitioner in 1930, and the balance of $952.00 is allocable to the stock sold by petitioner in 1931.

VIII

In his Federal income tax return for the calendar year 1939, the petitioner reported income of only $157.04 on account of the receipt of said $33,404. In the deficiency notice from which the appeal herein was taken, the respondent adjusted the amount of the income reported by the peti-

tioner on said recovery by adding $33,246.96 thereto, thereby treating the entire amount of petitioner's net recovery of $33,404 as gross income 100% taxable.

IX

If the entire deduction of $62,271.00 which was allowed as a deduction in connection with petitioner's 1930 Federal income tax liability had been disallowed, a deficiency in petitioner's Federal income tax liability for 1930 would have resulted in the amount of $1,232.75, computed as follows:

Net loss per R. A. R., May 27, 1932		($30,043.47)
Add:		
Loss on National City Bank stock, eliminated		62,271.00
Net income revised		32,227.53
Less:		
Dividends	$23,659.45	
Personal exemption	3,500.00	
Credit for dependents	1,200.00	
		28,359.45
		3,868.08
Normal tax: 1½ of $3,868.04		57.02
Surtax on $32,227.53		1,240.48
Total		1,297.50
Less:		
Earned income credit		64.75
Total tax assessable		1,232.75
Assessed		0.00
Deficiency		1,232.75

Throughout the year 1939 assessment of this deficiency was barred by the statute of limitations.

X

If the petitioner had received $32,294.96 on the sale of the stock in 1930 in addition to the amount of $20,897.44

[fol. 78] which he actually received, his 1930 deductible loss from the sale of said stock would have been $29,976.04 and his Federal income tax liability for 1930 would have been zero computed as follows:

Net loss per R. A. R. May 27, 1932		(30,043.47)
Add:		
Entire amount recovered in 1939 in reduction of loss on stock sold in 1930		32,294.96
Net income revised		2,251.49
Less:		
Dividends	$23,659.45	
Personal exemption	3,500.00	
Credit for dependents	1,200.00	
Total		28,359.45
Balance subject to normal tax		none
Total tax assessable		none
Tax assessed		none
Deficiency		none.

XI

On or about March 15, 1932, petitioner filed an income tax return for the calendar year 1931 with the Collector of Internal Revenue of the United States, in and for the District of Minnesota. In said return, petitioner disclosed net income of $17,514.27, and a tax thereon of $125.43 which was paid to the Collector of Internal Revenue during the calendar year 1932. The petitioner did not claim the deduction in said return by reason of the loss upon the sale of 200 shares of stock of National City Company realized by petitioner as set forth in Paragraph V supra. Had said loss been claimed by the petitioner, it would have been allowed by the respondent and would have reduced the income liability of petitioner for the calendar year 1931 but would not have eliminated it entirely. Except for the failure to deduct a loss on the sale of said 200 shares of stock of National City Bank, the income deductions and credits set forth in said return were true and correct and the respondent has not made any changes therein.

XII

Photostats of petitioner's Federal income tax returns for the calendar years 1930, 1931 and 1939 are attached hereto, marked Exhibits C, D and E respectively, and made a part hereof the same as if fully set forth herein. The income deductions and credits for the year 1930 are true [fol. 79] and correct as adjusted in the copy of the Revenue Agent's report which is attached to Exhibit C as a part thereof.

Leland W. Scott, John W. Windhorst, Counsel for Petitioner. (Signed) J. P. Wenchel, D. A. T., Chief Counsel, Bureau of Internal Revenue, Counsel for Respondent.

UNITED STATES CIRCUIT COURT OF APPEALS, EIGHTH CIRCUIT

B. T. A. Docket No. 106553

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, Petitioner,

v.

JOHN V. DOBSON, Respondent

JOHN V. DOBSON, Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent

JOINT DESIGNATION OF RECORD FOR REVIEW

To the Clerk of the United States Board of Tax Appeals:

You are requested by petitioners in the above-entitled action to prepare, transmit, and deliver to the Clerk of the United States Circuit Court of Appeals for the Eighth Circuit copies, duly certified as correct, of the following documents and records in the above-entitled cause in connection with the Petitions for Reivew heretofore filed by the respective petitioners:

1. Docket entries of proceedings before the Board.
2. Pleadings before the Board.
3. Opinion of the Board promulgated March 27, 1942.

4. Decision entered April 22, 1942.

5. Petition for Review and Statement of Points filed on July 10, 1942, by petitioner, Guy T. Helvering, Commissioner of Internal Revenue, together with notice of filing thereof and proof of service.

[fol. 80] 6. Petition for Review and Statement of Points filed on July 20, 1942, by petitioner, John V. Dobson, together with notice of filing thereof and proof of service.

7. The stipulation of facts agreed upon between the parties.

8. This Designation of Record.

(S.) J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue. Attorney for Guy T. Helvering, Commissioner of Internal Revenue. (S.) Leland W. Scott, John W. Windhorst, Attorneys for Petitioner, John V. Dobson.

UNITED STATES BOARD OF TAX APPEALS, WASHINGTON

Docket No. 106553

COMMISSIONER OF INTERNAL REVENUE, Petitioner,

v.

JOHN V. DOBSON, Respondent

Docket No. 106553

JOHN V. DOBSON, Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent

CERTIFICATE

I, B. D. Gamble, clerk of the U. S. Board of Tax Appeals, do hereby certify that the foregoing pages, 1 to 76, inclusive, contain and are a true copy of the transcript of record,

papers, and proceedings on file and of record in my office as called for by the Praecipe in the appeal (or appeals) as above numbered and entitled.

In testimony whereof, I hereunto set my hand and affix the seal of the United States Board of Tax Appeals, at Washington, in the District of Columbia, this 25th day of August 1942.

B. D. Gamble, Clerk, United States Board of Tax Appeals. (Seal.)

[fol. 81] IN THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE EIGHTH DISTRICT

[Title omitted]

September 10, 1942.

ORDER CONSOLIDATING CASES FOR BRIEFING, HEARING, ARGUMENT AND DECISION AND AS TO PRINTING OF RECORDS

Come now the parties to the above entitled proceedings, by their counsel of record, and it is

[fol. 82] Ordered, that the above enttiled proceedings be consolidated for briefing, hearing, argument and decision; that one brief shall be filed on behalf of the Commissioner and one on behalf of the four taxpayers; that the first brief shall be filed by the Commissioner and that it shall be filed within forty days after the date on which the last transcript of record is filed with the Clerk of this Court in the cases in which the Commissioner has filed petitions for review; that the second brief shall be filed on behalf of the taxpayers twenty-five days after their receipt of the Commissioner's brief, in accordance with the rules of this Court; that in order to facilitate handling of these proceedings and also to provide a fair and practicable method of dividing costs, the transcripts of record in the three cases appealed by the Commissioner shall be consolidated for printing and be printed by the Commissioner when his brief is printed; that such record shall include, in the case of John V. Dobson, all the material needed to consider both of the issues referred to above with the exception of

the cross-petition for review which shall be printed as hereinafter indicated; that the transcript of record in H. J. Harwick v. Commissioner and the cross-petition in the case of John V. Dobson shall be printed together by the taxpayers therein with the cost of printing to be divided between them as they shall decide; and that the latter record shall be printed by the taxpayers in sufficient time for it to be available for use by counsel for Commissioner in preparation of his brief, or they shall furnish a copy of the record to be printed to counsel for Commissioner in ample time for his use.

September 10, 1942.

[fol. 83] Appearances of counsel omitted in printing

[fol. 84] IN UNITED STATES CIRCUIT COURT OF APPEALS, EIGHTH CIRCUIT

[Title omitted]

ORDER OF SUBMISSION—January 6, 1943

[fol. 85] These causes, Nos. 12421, 12425, 12426, 12429 and 12430, having been called for hearing in their regular order, are argued together, and argument was commenced by Mr. John W. Windhorst for the Taxpayers, continued by Mr. S. Dee Hanson, Special Assistant to Attorney General, for Guy T. Helvering, Commissioner of Internal Revenue, and concluded by Mr. John W. Windhorst for the Taxpayers.

Thereupon, these causes were submitted to the Court on the abstract and transcripts of records and the briefs of counsel filed herein.

[fol. 86] In United States Circuit Court of Appeals, Eighth Circuit, March Term, A. D. 1943

No. 12,421

H. J. Harwick, Petitioner,

vs.

Commissioner of Internal Revenue, Respondent

No. 12,425

Guy T. Helvering, Commissioner of Internal Revenue, Petitioner,

vs.

John V. Dobson, Respondent

No. 12,426

John V. Dobson, Petitioner,

vs.

Guy T. Helvering, Commissioner of Internal Revenue, Respondent

No. 12,429

Guy T. Helvering, Commissioner of Internal Revenue, Petitioner,

vs.

Estate of James N. Collins, Deceased, First National Bank and Trust Company of Minneapolis, Executor, Respondent

No. 12,430

Guy T. Helvering, Commissioner of Internal Revenue, Petitioner,

vs.

E. W. Dobson, Respondent

Petitions to Review Decisions of United States Board of Tax Appeals

[fol. 87] Mr. S. Dee Hanson, Special Assistant to the Attorney General (Mr. Samuel O. Clark, Jr., Assistant Attorney General, Mr. Sewall Key, Miss Helen R. Carloss and Miss Louise Foster, Special Assistants to the Attorney General, were on the brief), for the Commissioner of Internal Revenue.

Mr. John W. Windhorst (Mr. Leland W. Scott and Messrs. Fletcher, Dorsey, Barker, Colman & Barber were with him on the brief) for the Taxpayers.

Before Sanborn, Woodrough and Thomas, Circuit Judges

OPINION—March 2, 1943

THOMAS, Circuit Judge, delivered the opinion of the court.

These cases come here upon petitions to review decisions of the United States Board of Tax Appeals. By order of court they have been consolidated for briefing, hearing, argument and decision.

Several years before the taxable year 1939, the four taxpayers, all residents of the state of Minnesota, had at various times individually purchased, in transactions entered into for profit, shares of the capital stock of the National City Bank of New York, such stock carrying beneficial interests in the stock of the National City Company of New York. The purchases were made in the state of Minnesota from the National City Company. Each taxpayer sold a part or all of such stock at losses which were claimed and allowed as deductions on their income tax returns for 1930 and 1931.

On a sale of 200 shares E. W. Dobson in 1930 deducted a loss of $49,302.56 and his return showed a net loss of $30,197.56; John V. Dobson for sales in 1930 deducted $62,271 and showed in his return a net loss of $30,043.47; [fol. 88] James N. Collins deducted and was allowed $41,600.80 for 1930 and $28,163.78 for 1931 and his net loss for these years was $65,896.51 and $40,204.90, respectively; and H. J. Harwick was allowed a deduction in 1931 for a loss of $34,451.28, and he reported a net income of $12,042.03, but due to certain credits he owed no tax.

For several years the taxpayers regarded these purchases and sales as completed transactions. In 1936, 1937 and 1938 they learned for the first time that the stock had not been registered under the Blue Sky laws of Minnesota and that the sales to each of them may have ben fraudulent. Thereupon H. J. Harwick asserted a claim against the National City Company, and the other three taxpayers filed suits against the Company alleging (1) that the stock sold had not been registered as required by law and (2) that the sales had been fraudulent. They requested rescission of the sale contracts and offered to turn over to the Company the proceeds of the stock sales or an equal number of shares plus interest and dividends received.

Harwick's claim and the suits were all settled in 1939. In the settlement Harwick received a net amount of $17,000 and reported $9,884.22 as income, conceding that he had

received a tax benefit for that amount in 1931. He contended that the remaining $7,115.78 should not be taxed, because he could have added this amount to his 1931 gross income without tax liability resulting for the reason that credits to which he was entitled more than offset his net income. E. W. Dobson received $31,432.80; John V. Dobson $32,294.96; and James N. Collins $23,296.45, all of which recoveries were allocable to 1930 sales. Collins also received $6,454.18 allocable to a 1931 sale. Neither the Dobsons nor Collins reported any part of these sums as income in 1939, but the Commissioner included them all, as well as the $7,115.78 received by Harwick.

[fol. 89] Through the year 1939 adjustment of the taxpayers' income tax liability for the years deductions were claimed and allowed was barred by the statute of limitations.

The Board held that the recoveries in 1939 were in the nature of a capital recovery and were not subject to tax, unless the loss deductions of the prior years had actually offset gross income of those years and had thus resulted in a tax benefit. On this theory the Board held that E. W. Dobson and James N. Collins having realized no tax benefit from the loss deductions in 1930 and 1931, the sums recovered by them in 1939 were not taxable; that John V. Dobson having realized a tax benefit on $2,251.49, that sum was taxable in 1939 as ordinary income and was not capital gain; and that Harwick, having a net income in 1931, received a tax benefit on the entire recovery and that it should be included in his 1939 return.

The opinion of the Board in John V. Dobson's case is reported in 46 B. T. A. 770, and that of the Estate of James N. Collins in 46 B. T. A. 765. Opinions in the other cases are not officially reported.

The Commissioner contends that the recoveries of the taxpayers in 1939 relative to deductions claimed and allowed in 1930 and 1931 should all be included in their gross incomes for the year 1939 under § 22 of the Internal Revenue Code and taxed as ordinary income, and that the Board erred in refusing so to hold and in refusing to redetermine a deficiency in the case of E. W. Dobson in the amount of $7,490.86; in the case of John V. Dobson in the amount of $9,108.06; and in the case of the estate of James N. Collins in the amount of $2,644.58.

The taxpayers all contend that the Board correctly held that the taxability of the recoveries in 1939 depends on

whether the 1930 and 1931 deductions attributable to sales [fol. 90] of stock resulted in a tax benefit. Harwick and John V. Dobson in their appeals contend that the Board erred in holding that a tax benefit depends upon whether the losses produced a deficit in the taxpayers' net income for 1930 and 1931. They urge that a tax benefit depends on an actual saving in tax dollars for those years. All the taxpayers assert that to whatever extent taxable gain is found to exist by reason of the 1939 recoveries, such income is taxable as capital gain under § 117 of the Internal Revenue Code and not as ordinary income under § 22.

As a result of the Board's refusal to accept the contentions of the several taxpayers, Harwick contends that it erred in failing to order a refund to him in the amount of $2,914.84 on account of the inclusion in his 1939 return of gross income in the sum of $9,884.22 reported by him as ordinary income in that year, and in redetermining a deficiency of $4,629.01 for 1939. John V. Dobson contends that the Board erred in redetermining a deficiency in his income-tax liability for 1939 in the amount of $472.82 as a result of including $2,251.49 of his recovery in gross income for that year; and that, if such sum should be included, it should be taxed as capital gain and not as ordinary income.

A fact characteristic of all these cases is that the purchase price paid for the stock by each taxpayer was in excess of the proceeds received by him from the sale of the stock in 1930 and 1931 and the recovery from the National City Company in 1939 combined. As a whole the stock investment was a losing venture. The cases present only questions of law.

The first matter to be determined is the question of the validity of the tax benefit theory applied by the Board to [fol. 91] the taxability of the recovery in the taxable year of a capital loss sustained, and claimed and allowed as a deduction, in a prior year.

The conclusion of the Board and its reason therefor are stated in its opinion in the John V. Dobson case (46 B. T. A. 770) in the following language:

"Where there is recovery in respect of a loss sustained in an earlier year and a deduction of such loss claimed and allowed for the earlier year had effected an offset in taxable income, the amount recovered in the later year should be included in taxable income for the year of recovery, the

reason being that even though the subsequent recovery is in the nature of a capital recovery the prior deduction of the amount of the loss from taxable income has for income tax purposes already given the taxpayer a recoupment of said loss out of taxable income and the subsequent recovery, being in the nature of a replacement of taxable income, is equivalent to gain to the taxpayer. *National Bank of Commerce of Seattle* v. *Commissioner,* 115 F. 2d 875, affirming 40 B. T. A. 72. But where the deduction claimed and allowed in the prior year did not effect an offset of taxable income, the amount recovered in a later year does not constitute taxable income for the year of recovery."

The Board's explanation of its decision is not found in the Revenue Acts in effect in 1930, in 1931, or in 1939, nor in any of the regulations thereunder. The taxpayers, however, relying upon the decision of the Supreme Court in *Eisner* v. *Macomber,* 252 U. S. 189, 206, say that for constitutional reasons the tax cannot be sustained at all, unless it be upon the tax benefit theory. It is urged that there is no magic sufficient to convert capital into income for tax purposes. They argue that if there be such "magic" it is found in and limited in its application by some form of offset or recoupment.

[fol. 92] We are of the opinion that the constitutional question discussed in the Macomber case is not presented in these cases. Decision depends upon the application of well-settled principles of tax laws. The losses here were claimed and allowed pursuant to the privilege granted under § 23(e)(2) of the Revenue Act of 1928, c. 852, 45 Stat. 791, 26 U. S. C. A. Internal Revenue Acts. The pertinent part of the Act provides that in computing net income there shall be allowed as deductions, "In the case of individuals, losses sustained during the taxable year—* * * (2) if incurred in any transaction entered into for profit, though not connected with the trade or business."

The adoption of the tax benefit theory seems to be an injection into the law of an equitable principle, found neither in the statutes nor in the regulations, for the purpose apparently either of avoiding constitutional restrictions or of granting to the taxpayer relief in hard cases. In *Deputy* v. *du Pont,* 308 U. S. 488, 493, the Supreme Court said: "* * * allowance of deductions from gross income does not turn on general equitable considerations. It 'depends upon legislative grace.'" Citing *New Colon-*

ial Ice Co. v. *Helvering,* 292 U. S. 435, 440. See, also *Citizens National Bank* v. *Commissioner,* 8 Cir., 122 F. 2d 1011, 1013; *White* v. *United States,* 305 U. S. 281, 292; *Helvering* v. *Insurance Co.,* 294 U. S. 686, 689. It follows that when deductions for losses are taken, they can be taken on such conditions only as the government prescribes.

When the taxpayers here claimed and were allowed the deductions for losses on sales of stock in 1930 and 1931 under § 23(e) (2), supra, at least three conditions inhered in the allowance. First, any future adjustment or corrections were subject to the statute of limitations. Revenue Act of 1928, § 275(a). Second, Article 342 of Treasury Regulations 74, promulgated under the Revenue Act of [fol. 93] 1928, provided that "The expenses, liabilities or deficit of one year can not be used to reduce the income of a subsequent year." The regulation is consistent with the rule that the federal income tax system is based on an annual accounting. *Burnet* v. *Sanford & Brooks Co.,* 282 U. S. 359, 365; *Burnet* v. *Thompson Oil & Gas Co.,* 283 U. S. 301, 306; *Woolford Realty Co.* v. *Rose,* 286 U. S. 319, 326; *Brown* v. *Helvering,* 291 U. S. 193, 198-9; *Helvering* v. *Morgan's, Inc.,* 293 U. S. 121, 126-7; *Guaranty Trust Co.* v. *Commissioner,* 303 U. S. 493, 497-8; *Heiner* v. *Mellon,* 304 U. S. 271, 275. A third condition of the allowance of deductions for capital losses under the Revenue Act of 1928, as well as of the earlier and later Revenue Acts, is the requirement that such losses must be "realized" by some closed and completed "identifiable event" which definitely settles and determines the existence of and the amount of such losses. *Schoenberg* v. *Commissioner,* 8 Cir., 77 F. 2d 446, 448, and cases cited. See, also, *Higgins* v. *Smith,* 308 U. S. 473, 481.

The contention of the taxpayers requires these three conditions of the revenue laws to be evaded or ignored. The statute of limitations will be evaded by adjusting deductions in 1939 on the basis of equitable considerations resulting from events occurring in 1930 and 1931. Treasury Regulation 74 will be violated by using the deficits of one taxable year to reduce the income of a subsequent year; and a capital transaction represented by the taxpayer to be "closed and completed" in 1930 and 1931 must be reopened in 1939 in violation of all three of the conditions stated above. There is no escape under the law from the fact that the capital transactions of the taxpayers were

closed and their capital losses claimed and allowed in the years when the stocks were sold. The recoveries received in 1939 resulting from discovered fraud in the original [fol. 94] purchases were income in the year received. It is immaterial whether the claim was settled before suit, as in Harwick's case, or after suit was begun; and it is immaterial whether the taxpayer invoked as a remedy for fraud the right to rescission or the right to damages. In any case the recovery was income when received. Any diminution of gross income in 1939 because of lack of complete tax benefits from the deductions taken in 1930 and 1931 constitutes in reality a deduction in 1939 based upon equitable considerations and not upon the authority of an Act of Congress.

The circumstances in the case of *Griffiths* v. *Commissioner*, 308 U. S. 355, are so strikingly similar to the facts in this case that the decision illustrates the accepted view of the law, even though the tax benefit theory was not discussed. Griffiths, the taxpayer, paid one Lay $100,000 for some stock in 1926. The investment was unprofitable, and as the result of the sale of the stock to a family corporation Griffiths was allowed a deductible loss of $92,500 by the Commissioner for the year 1931. In 1933 Griffiths learned that he had been defrauded by Lay in the 1926 sale. Through a settlement with Lay in 1933 the stock, through a complicated series of transactions entered into to disguise the rescission of the original purchase, was transferred back to Lay and Griffiths personally received, from Lay $100,000. The Commissioner ruled that Griffiths, having been allowed a deduction for loss attributable to the stock purchased from Lay and having now recouped that loss through settlement of his claim against Lay, was subject to tax for the amount of the settlement in 1933. The Supreme Court held that "the Commissioner was right", and affirmed the decision of the Seventh Circuit Court of Appeals (103 F. 2d 110).

[fol. 95] Since the Board decided these cases the question of the application of the equitable doctrine involved in the tax benefit theory has been passed upon by the Third and Fourth Circuit Courts of Appeals in cases involving the recovery of bad debts and decided adversely to the theory of the Board and the contentions of the taxpayers. *Helvering* v. *State-Planters Bank & Trust Co., 4 Cir.*, 130 F. 2d 44; *Commissioner* v. *United States & International Securities*

Corporation, 3 Cir., 130 F. 2d 894. In the first of these cases Judge Parker, speaking for the court, observed that "There is nothing in the regulation or in any statute which makes the inclusion, in gross income of collections on bad debts, previously charged off as worthless, dependent upon whether or not the charge off has resulted in a tax benefit to the taxpayer." The court held that when the taxpayer charges off and is allowed a deduction for a bad debt in one year, he thereby under the existing regulations impliedly consents that a subsequent recovery shall be treated as income and not as a restoration of capital. In substance it was held that a taxpayer who obtains the allowance of a deduction for a bad debt, or capital loss, under a statute permitting such privilege, is bound by a regulation providing that any subsequent recovery of any part of such bad debt "must be included in gross income for the taxable year in which received."

These decisions are in agreement with *Stearns Coal & Lumber Co.* v. *Glenn, Collector*, D. C. Ky., 42 F. Supp. 28. The only case cited by the taxpayers reaching a contrary conclusion is that of *Philadelphia National Bank* v. *Rothensies*, D. C. Penn., 43 F. Supp. 923, in which it was held that the implied consent of the taxpayer, in the absence of express terms, cannot "be carried beyond the benefit received."

[fol. 96] We think the allowance of deductions from gross income cannot be made to depend upon general equitable considerations, such as are involved in the tax benefit theory; and that the taxpayers are barred by the conditions on which the government granted the deductions in the earlier years.

For the foregoing reasons we hold that the recoveries of the taxpayers in 1939, allocable to the sales of stock in 1930 and 1931, constitute taxable gain in the year received.

Harwick and John V. Dobson do not agree with the Board in the application of the tax benefit theory to their cases, but, since we hold that the tax benefit theory must be rejected entirely, it is unnecessary to discuss their contentions in this respect.

In view of our conclusion above there remains for consideration only the question whether the 1939 recoveries must be treated as ordinary income under § 22 or as long-term capital gains under § 117 of the Internal Revenue

Code.[1] Under the latter section only fifty per cent of the recoveries would be taxable.

[fol. 97] The question to be determined is whether the payments to the taxpayers by the National City Company in settlement of their claims constitute gain realized in a "sale or exchange" of a capital asset. It is not contended that an actual sale or exchange occurred in 1939 upon the settlement of the taxpayer's claims, but that the payments in 1939 take their character as capital gain from the sales of the stock in 1930 and 1931. This conclusion is arrived at in this way. It is said (1) that the taxpayers' claims against the National City Company were based on the right to rescind the stock purchase and to secure a refund of the purchase price; (2) that the Commissioner admits that where a taxpayer had not sold his stock the recovery in 1939 attributable to such unsold stock was not taxable; and (3) that, therefore, the receipt of income in 1939 (to whatever extent taxable) represented "gain from the sale" of the stock in 1931 which was not taxable until received in 1939.

The contention lacks merit. The Commissioner did not admit that deductions which had been claimed and allowed as a result of sales in 1930 and 1931 could be converted into non-taxable recoveries in 1939. There was no causal relation between the sales in the former years and the recoveries in the latter. The sales of stock and the settle-

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[1] Section 22 of the Internal Revenue Code, 26 U. S. C. A. 22, provides:

"Gross income" includes gains, profits, and income derived from * * * trades, business, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever.

Section 117 (a) provides:

(4) *Long-term capital gain.* The term "long-term capital gain" means gains from the sale or exchange of a capital asset held for more than 18 months, if and to the extent such gain is taken into account in computing net income;

(5) *Long-term capital loss.* The term "long-term capital loss" means loss from the sale or exchange of a capital asset held for more than 18 months, if and to the extent such loss is taken into account in computing net income.

ments of the claims were different and distinct transactions. The settlements considered separately were neither sales nor exchanges within the meaning of the statute. *Lee* v. *Commissioner*, 7 Cir., 119 F. 2d 946; *Bingham* v. *Commissioner*, 2 Cir., 105 F. 2d 971; *Hale* v. *Helvering*, App. D. C., 85 F. 2d 819. The taxpayers sold nothing in 1939 to the National City Company and the National City Company purchased nothing from the taxpayers. Neither was there an exchange, for "exchange", as used in the statute, means reciprocal transfers of capital assets. [fol. 98] *Helvering* v. *Flaccus Leather Co.*, 313 U. S. 247, 249. The sales of stock were completed transactions in 1930 and 1931, and they can neither in fact nor in law be coupled with the settlements in 1939 so as to transform the two events into a single sale or exchange of capital assets. The Board was right in holding that the recoveries in 1939 were taxable as ordinary income and not as long-term capital gains.

The decision of the Board in No. 12,421, Harwick v. Commissioner, is affirmed.

In No. 12,430, Helvering v. E. W. Dobson, and in No. 12,429, Helvering v. Estate of James N. Collins, the decisions are reversed and the cases remanded with instructions to tax as ordinary income the entire recoveries attributable to the losses claimed and allowed in previous years.

In the John V. Dobson cases, Nos. 12,425 and 12,426, the decision is reversed and the cases remanded with instructions to tax as ordinary income the entire amount recovered in 1939 attributable to the loss claimed and allowed in 1930.

[fol. 99] IN UNITED STATES CIRCUIT COURT OF APPEALS, EIGHTH CIRCUIT, MARCH TERM, 1943

No. 12421

H. J. HARWICK, Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE

On Petition to Review Decision of United States Board of Tax Appeals

JUDGMENT—March 2, 1943

This cause came on to be heard on the petition to review the decision of the United States Board of Tax Appeals

entered April 23, 1942, deciding that there is a deficiency in income tax of the Taxpayer for the year 1939, and was argued by counsel.

On Consideration Whereof, It is now here Ordered and Adjudged by this Court that the decision of the said Board of Tax Appeals in this cause be, and the same is hereby, affirmed.

And it is further Ordered by this Court that the petition to review herein be, and the same is hereby, dismissed without the taxation of costs in this Court in favor of either of the parties.

March 2, 1943.

[fol. 100] IN UNITED STATES CIRCUIT COURT OF APPEALS, EIGHTH CIRCUIT, MARCH TERM, 1943

No. 12425

GUY T. HELVERING, Commissioner of Internal Revenue, Petitioner,

vs.

JOHN V. DOBSON

No. 12426

JOHN V. DOBSON, Petitioner,

vs.

GUY T. HELVERING, Commissioner of Internal Revenue

JUDGMENT—March 2, 1943

On Petitions to Review Decision of the United States Board of Tax Appeals

These causes came on to be heard on the petitions filed by Guy T. Helvering, Commissioner of Internal Revenue, and by John V. Dobson to review the decision of the United States Board of Tax Appeals entered April 22, 1942, deciding that there is a deficiency in income tax of the Taxpayer for the year 1939, and were argued by counsel.

On Consideration Whereof, It is now here Ordered and Adjudged by this Court that the decision of the said Board of Tax Appeals in these causes be, and the same is hereby, reversed without taxation of costs in favor of either of the parties in this Court.

And it is further Ordered by this Court that these causes be, and they are hereby, remanded to The Tax Court of the United States as the successor of the United States Board [fol. 101] of Tax Appeals with instructions to tax as ordinary income the entire amount recovered in the year 1939 attributable to the loss claimed and allowed in the year 1930.

March 2, 1943.

[fol. 102] In United States Circuit Court of Appeals, Eighth Circuit, March Term, 1943

No. 12429

Guy T. Helvering, Commissioner of Internal Revenue, Petitioner,

vs.

Estate of James N. Collins, Deceased, First National Bank and Trust Company of Minneapolis, Executor

Judgment—March 2, 1943

On Petition to Review Decision of United States Board of Tax Appeals

This cause came on to be heard on the petition to review the decision of the United States Board of Tax Appeals entered April 25, 1942, deciding that there is no deficiency in income tax of the Taxpayer for the year 1939, and was argued by counsel.

On Consideration Whereof, It is now here Ordered and Adjudged by this Court that the decision of the said Board of Tax Appeals in this cause be, and the same is hereby, reversed without taxation of costs in favor of either of the parties in this Court.

And it is further Ordered by this Court that this cause be, and it is hereby, remanded to The Tax Court of the United States as the successor of the United States Board of Tax Appeals with instructions to tax as ordinary income the entire recoveries attributable to the losses claimed and allowed in previous years.

March 2, 1943.

[fol. 103] IN UNITED STATES CIRCUIT COURT OF APPEALS, EIGHTH CIRCUIT

No. 12430—March Term, 1943

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, Petitioner,

vs.

E. W. DOBSON

ON PETITION TO REVIEW DECISION OF UNITED STATES BOARD OF TAX APPEALS

JUDGMENT—March 2, 1943

This cause came on to be heard on the petition to review the decision of the United States Board of Tax Appeals entered March 30, 1942, deciding that there is no deficiency in income tax of the Taxpayer for the year 1939, and was argued by counsel.

On Consideration Whereof, It is now here Ordered and Adjudged by this Court that the decision of the said Board of Tax Appeals in this cause be, and the same is hereby, reversed without taxation of costs in favor of either of the parties in this Court.

And it is further Ordered by this Court that this cause be, and it is hereby, remanded to The Tax Court of the United States as the successor of the United States Board of Tax Appeals with instructions to tax as ordinary income the entire recoveries attributable to the losses claimed and allowed in previous years.

March 2, 1943.

[fol. 104] IN UNITED STATES CIRCUIT COURT OF APPEALS

MOTION OF TAXPAYERS FOR STAY OF MANDATES—Filed March 18, 1943

Now come the above named taxpayers, by John W. Windhorst, their attorney, and respectfully move this Honorable Court to stay and withhold its mandate in the above entitled actions for the purpose of permitting said taxpayers to file with the Clerk of the Supreme Court of the United

States their petitions for writs of certiorari in said causes until and including the 16th day of April, 1943, and to order that the stay of said mandates be continued if, on or before said date, said petitions are filed and the Clerk of this court receives from the Clerk of the Supreme Court his certificates of said filing until the final disposition of said causes by the Supreme Court of the United States, all as provided by Rule 16 of this Court.

Dated March 17, 1943.

John W. Windhorst, Attorney for Taxpayers, 1300 First National-Soo Line Bldg., Minneapolis, Minnesota.

Leland W. Scott and Dorsey, Colman, Barker, Scott & Barber, of Counsel.

[File endorsement omitted.]

[fol. 105] ORDER STAYING ISSUANCE OF MANDATES

Memorandum of Clerk of U. S. Circuit Court of Appeals for the Eighth Circuit:

Orders were entered in the within cases staying issuance of mandates on motion of taxpayers and all orders are alike except that they are either on motion of petitioner, taxpayer or respondent. With this exception each order is in the following words:

March Term, 1943.
Saturday, March 20, 1943.

On Consideration of the motion of the petitioner for a stay of the mandate in this cause pending a petition to the Supreme Court of the United States for a writ of certiorari, It is now here ordered by this Court that the issuance of the mandate herein be, and the same is hereby, stayed for a period of thirty days from and after this date, and if within said period of thirty days there is filed with the Clerk of this Court a certificate of the Clerk of the Supreme Court of the United States that a petition for writ of certiorari, record and brief have been filed, the stay hereby granted shall continue until the final disposition of the case by the Supreme Court.

March 20, 1943.

[fols. 106-107] Clerk's Certificate to foregoing transcript omitted in printing.

[fol. 108] SUPREME COURT OF THE UNITED STATES

No. 44—October Term, 1943

ORDER ALLOWING CERTIORARI—Filed June 14, 1943

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Eighth Circuit is granted, and the case is transferred to the summary docket.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

[fol. 109] SUPREME COURT OF THE UNITED STATES

No. 45—October Term, 1943

ORDER ALLOWING CERTIORARI—Filed June 14, 1943

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Eighth Circuit is granted, and the case is transferred to the summary docket.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

[fol. 110] SUPREME COURT OF THE UNITED STATES

No. 46—October Term, 1943

ORDER ALLOWING CERTIORARI—Filed June 14, 1943

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Eighth Circuit is granted, and the case is transferred to the summary docket.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

[fol. 111] SUPREME COURT OF THE UNITED STATES

No. 47—October Term, 1943

ORDER ALLOWING CERTIORARI—Filed June 14, 1943

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Eighth Circuit is granted, and the case is transferred to the summary docket.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

[Endorsed on Cover:] File No. 47,431, 47,432, 47,433, 47,434, U. S. Circuit Court of Appeals, Eighth Circuit. Term No. 44, John V. Dobson, Petitioner, vs. Guy T. Helvering, Commissioner of Internal Revenue. Term No. 45, E. W. Dobson, Petitioner, vs. Guy T. Helvering, Commissioner of Internal Revenue. Term No. 46, Estate of James N. Collins, Deceased, First National Bank and Trust Company of Minneapolis, Executor, Petitioner vs. Guy T. Helvering, Commissioner of Internal Revenue. Term No. 47, H. J. Harwick, Petitioner, vs. Commissioner of Internal Revenue. Petition for writs or certiorari and exhibit thereto. Filed April 15, 1943. Term No. 44 O. T. 1943, 45 O. T. 1943, 46 O. T. 1943, 47 O. T. 1943.